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HAROLD B. WILLEY, C

IN THE

Supreme Court of the United States

OCTOBER TERM, 1955

No. 584

FRANK GENTLES, DON F. GATES, RANDOLPH CALDWELL and FRANCIS V. NIXON,

Appellants,

vs.

F. BRITTON McCONNELL, as Insurance Commissioner of the State of California, F. BRITTON McCONNELL, Insurance Commissioner of the State of California, as Liquidator of The Pacific Mutual Life Insurance Company of California, and PACIFIC MUTUAL LIFE INSURANCE COMPANY, a California corporation,

Appellees.

ON APPEAL FROM THE SUPREME COURT OF THE STATE OF CALIFORNIA

JURISDICTIONAL STATEMENT

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INDEX

	PAGE
Opinions Below	2
Jurisdiction	2
Questions Presented	3
Statement of Facts	5
1. Parties	5
2. Seizure of Old Company in 1936; Creation of New Company; 1936 Rehabilitation Agreement	5
3. Mutualization provisions of Rehabilitation Agreement	8
4. Mutualization proceedings	9
5. Finding as to practicability of mutualization	10
6. Fixing of the Purchase Price	11
7. Provisions for payment of purchase price	14
8. Proceedings Below	15
9. Res Judicata	21
Substantial constitutional questions are raised on this appeal	22
Substantive due process	22
Procedural due process	35
Conclusion	40

DEC 24 1957

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CITATIONS

PAGE

CASES:

Alabama Comm. v. *Southern R. R.*, 341 U. S. 341.. 38
Application of Prudential Insurance Company, 132 N. J. Eq. 170 22
Atchison R. R. v. *Pub. Util Comm*, 346 U S. 346 3

Backus v. *Fort Street Union Depot Co.*, 169 U. S. 568 25
Belden v. *Union Central Life Insurance Co.*, 143 Ohio St. 329 22
Buchanan v. *Warley*, 245 U. S. 60 26

Caminetti v. *Pacific Mut. L. Ins. Co.*, 23 Cal. 2d 94 8
Caminetti v. *Pacific Mut. L. Ins. Co.*, 23 Cal. 2d 334 8
Carpenter v. *Pacific Mut. L. Ins. Co.*, 10 Cal. 2d 307 .....6, 7, 39
Carpenter v. *Pacific Mut. L. Ins. Co.* (not officially reported), Superior Court, Los Angeles County, December 3, 1936 6
Carpenter v. *Pacific Mut. L. Ins. Co.*, 13 Cal. 2d 306 8
Case v. *Los Angeles Lumber Co.*, 308 U. S. 106...21, 38
Cherokee Nation v. *Kansas R. R.*, 135 U. S. 641... 25
Connecticut Co. v. *Palmer*, 305 U. S. 493 35

Dahnke-Walker Co. v. *Bondurant*, 257 U. S. 282... 2
Doty v. *Love*, 295 U. S. 64 22

Ecker v. *Western Pacific R. R.*, 318 U. S. 448....23, 38
Eubank v. *Richmond*, 226 U. S. 137 22

Garrison v. *Pacific Mut. L. Ins. Co.*, 83 Cal. App. 2d 1 8

Hamilton v. *Regents*, 293 U. S. 245 3

In re Equitable Office Bldg. Corp., 96 L. Ed. 1386, not officially reported 23
In re Prudential Insurance Company, 82 N. J. Eq. 335 22

PAGE

Jacobs v. *United States*, 290 U. S. 13 29

Kelley v. *Everglades District*, 319 U. S. 415 38

Lake Erie & W. R. R. v. *Pub. Util. Comm.*, 249 U. S. 422 3
Live Oak Assn. v. *R. R. Commission*, 269 U. S. 354 3
Lord v. *Equitable Life Assurance Society*, 194 N. Y. 212 22
Louisville Bank v. *Radford*, 295 U. S. 555 30

Matter of Casualty Co. (Rubin Claim), 244 N. Y. 443 40
Matter of Globe & Rutgers Ins. Co., 148 Misc. 497 23
Matter of Lawyers Mortgage Co., 169 Misc. 802, *aff'd*, 256 App. Div. 974 40
Matter of Nemerov, 149 Misc. 797 40
Matter of New York Title & Mortgage Co., 171 Misc. 489 .....25, 40
Matter of New York Title & Mortgage Co., 168 Misc. 60 40
Monongahela Navigation Co. v. *United States*, 148 U. S. 312 25
Morgan v. *United States*, 298 U. S. 468 35

Nashville C. & St. L. R. R. v. *Walters*, 294 U. S. 405 2
Neblett v. *Carpenter*, 305 U. S. 297 .....6, 7
Neblett v. *Pacific Mut. L. Ins. Co.*, 22 Cal. 2d 393 8
Niagara Hudson Corp. v. *Leventritt*, 340 U. S. 336 38

Ohio Valley Co. v. *Ben Avon Borough*, 253 U. S. 287 37
Old Dearborn Co. v. *Seagram Corp.*, 299 U. S. 183 26
Olson v. *United States*, 292 U. S. 246 .....22, 25

Penn Co. v. *Pennsylvania*, 294 U. S. 189 38
Pennsylvania v. *Williams*, 294 U. S. 176 38
Phelps v. *United States*, 274 U. S. 341 29

RFC v. *Denver R. R.*, 328 U. S. 463 38
Rippel v. *Prudential Insurance Company*, 85 N. J. L. 395 22
St. Joe Paper Co. v. *Atl. Coast Line R. R.*, 347 U. S. 298 23
St. Joseph Stockyards Co. v. *United States*, 298 U. S. 38 38
Sanborn v. *Pacific Mut. L. Ins. Co.*, 42 Cal. App. 2d 99 8
Seaboard Air Line R. R. v. *United States*, 261 U. S. 299 29
SEC v. *Central-Illinois Corp.*, 338 U. S. 96 .....23, 38
Standard Oil Co. v. *Johnson*, 316 U. S. 481 2
Sweet v. *Rechel*, 159 U. S. 380 25
Thompson v. *Consolidated Gas Co.*, 300 U. S. 55... 26
Union Dry Goods Co. v. *Georgia P. S. Corp.*, 248 U. S. 372 22
United Railways v. *West*, 280 U. S. 234 38
United States v. *Westinghouse*, 339 U. S. 261..... 36
West Ohio Gas Co. v. *Comm.*, 294 U. S. 79..... 35

STATUTES:

Constitution of the United States, Amendment XIV 4, 21, 26, 37
U. S. C. Title 28, Section 1257(2).....2, 3, 22
California Code of Civil Procedure
Section 1094.5 .....2, 37
California Insurance Code
Section 986 6
Section 1037(e)..... 5
Section 1043 3
Sections 1045-56 3
Section 11525 16
Section 11526 16
Section 11527 .....16, 20
Sections 11525-27 .....3, 15, 35, 36

PAGE

Page's Ohio Code, Chapter 3913 37

MISCELLANEOUS:

Best's Life Insurance Reports, 1955 15

Davis, Administrative Law (1951), Chapter 19, "Nonreviewable Action" 39

Parish, The Mutualization of a Legal Reserve Stock Life Insurance Company, 11 Proc. of Assn. of Life Insurance Counsel 475, 479-483 (1952-1953) 37

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Appellees.

ON APPEAL FROM THE SUPREME COURT OF THE STATE OF CALIFORNIA

JURISDICTIONAL STATEMENT

This is an appeal from a judgment of the Supreme Court of California affirming (with three judges dissenting) a judgment of the Superior Court for Los Angeles County which denied a petition for a writ of mandate to review and set aside an order of the State Insurance Commissioner approving a plan for the mutualization of appellee Pacific Mutual Life Insurance Company (the "New Company").*

*This Jurisdictional Statement is filed on behalf of the appellants named in the caption. The other parties who have appealed from the judgment below have filed a separate Jurisdictional Statement.

Opinions Below

The opinion of the California Supreme Court and the two dissenting opinions are reported. 44 Cal. 2d 715, 285 P. 2d 636 (Appendix A). The opinion of the District Court of Appeal is reported. 270 P. 2d 584 (Appendix B). Neither the opinion of the Superior Court, filed March 24, 1952, nor that of the Insurance Commissioner, dated September 22, 1950, has been reported. They are printed as Appendices C and D.

Jurisdiction

(1) The proceeding below was brought under § 1094.5 of the California Code of Civil Procedure (App., E 12-14), which provides for review of administrative orders and decisions by writ of mandate.

(2) The date of the judgment of the California Supreme Court sought to be reviewed was June 27, 1955 (App. H). A petition by appellants for rehearing was denied without opinion, three judges dissenting, by order entered July 27, 1955. Notice of appeal to this Court was filed with the Clerk of the California Supreme Court on October 24, 1955.

(3) The jurisdiction of this Court is invoked under § 1257(2) of the Judicial Code, 28 U. S. C. § 1257(2).

(4) Cases believed to sustain the jurisdiction are *Dahnke-Walker Co.* v. *Bondurant,* 257 U. S. 282; *Standard Oil Co.* v. *Johnson,* 316 U. S. 481, and *Nashville C. & St. L. R. R.* v. *Walters,* 294 U. S. 405, holding that a proper case for appeal is presented where the validity of a state statute, as construed and applied, is drawn in question on the ground of repugnancy to the Federal Constitu-

tion; and *Lake Erie & W. R. R.* v. *Pub. Util. Comm.*, 249 U. S. 422; *Live Oak Assn.* v. *R. R. Commission*, 269 U. S. 354; *Hamilton* v. *Regents*, 293 U. S. 245; and *Atchison R. R.* v. *Pub. Util. Comm.*, 346 U. S. 346, holding that an order of a State administrative body or official, made in the exercise of delegated legislative authority, is a "statute" within the meaning of 28 U. S. C. § 1257(2).

(5) The validity of § § 11525-27 of the Insurance Code of California (App., E 9-12), as construed and applied in this case, is involved. Related statutes of California, the constitutionality of which is not involved, but which have a bearing on the case, are California Insurance Code § § 1043 and 1045-56. (App., E 1-9).* The validity of the Insurance Commissioner's order (App. D), as a statute within the meaning of 28 U. S. C. § 1257(2), is also involved.

Questions Presented

The Plan of Mutualization approved by the Insurance Commissioner provides for the purchase by the New Company of all its outstanding capital stock. It binds appellants, who are among the equitable owners of the stock, to a sale at a price determined as of 1948, but payment of which will not be made until the distant future, *i.e.*, between 1971 and 1983, if, as and when certain conditions precedent shall have been satisfied.

The questions presented are whether the order of the Commissioner, the judgment below and §§ 11525-27 of the California Insurance Code, as construed and applied in this case, deprive appellants of property without due process

*There is no official edition of the statutes of California.

of law contrary to Amendment XIV of the Constitution, (1) *substantively,* because the Plan of Mutualization:

(a) deprives appellants of the incidents of their equitable ownership of the stock, for a period that may extend to 1983, without compensation and without a definite and unconditional obligation to purchase and pay for the stock;

(b) does not provide for payment of the purchase price of the stock on the basis of its value at the time when the obligation to purchase and pay may arise, but permits the New Company to buy the stock at a remote future date, at a price equal to the value that the stock was determined to have had in 1948, plus interest at an inadequate and non-compensatory rate, all payable only if, at the time the obligation to pay may arise, the stock is worth many times the purchase price plus interest;

(c) fixes the purchase price upon a valuation arrived at by speculation and guesswork and upon assumptions having no rational basis in law or fact, and at an amount which is grossly inadequate and confiscatory; and

(2) *procedurally,* because:

(a) The order of the Commissioner approving the Plan of Mutualization is not supported by substantial or competent evidence and was not based upon a fair and open hearing before an impartial tribunal; and

(b) Appellants have not had an opportunity to submit to a judicial tribunal, for determination upon its own independent judgment as to law and fact, their claim that confiscation of their property will result if the Plan becomes effective.

Statement of Facts*

1. *Parties*

The New Company is the successor in rehabilitation of The Pacific Mutual Life Insurance Company of California (the "Old Company"), an appellant on the companion appeal. The appellants on whose behalf this Statement is filed are stockholders of the Old Company, who also are members of a protective committee representing some 60% of its total capital stock. The New Company is the proponent of the Plan of Mutualization. The appellee Commissioner is named both as Insurance Commissioner and in his capacity as Liquidator of the Old Company, in which capacity he owns the capital stock of the New Company as statutory trustee for the creditors and stockholders of the Old Company. Legal title to the stock was transferred to Voting Trustees in 1938, pursuant to a subdivision (e) added to § 1037 of the Insurance Code in 1937. The Commissioner is one of the Voting Trustees.

2. *Seizure of Old Company in 1936; Creation of New Company; 1936 Rehabilitation Agreement*

The Old Company in 1936 was an old-line, highly respected and successful insurance company, which had been organized in 1868, had written life, health and accident

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*The record on this appeal and the companion appeal is the same, and consists of four folders and certain numbered exhibits. References to "Tr." in this brief refer to Folder One, "Reporter's Transcript of proceedings before the Insurance Commissioner"; "Clk. Tr." to Folder Two, "Reporter's Transcript of proceedings in the Superior Court"; "Op. Br." to Appellants' Opening Brief in the District Court, "Pet. H." to their Petition for Hearing in the Supreme Court, and "Pet. Reh." to their Petition for Rehearing in the Supreme Court—all contained in Folder Three; and "Ex." followed by an arabic numeral to one of the separate numbered exhibits.

policies in California and many other States, and had assets in excess of $200,000,000. In spite of its name, it was a stock company, though it did write some life insurance upon a "participating basis". It had outstanding 508,200 shares of capital stock, distributed among some 3000 stockholders (App., A 21-23; App., D 1-3; Clk. Tr. 2).

The proceedings for rehabilitation of the business of the Old Company commenced in 1936, when the Insurance Commissioner, following a triennial audit of its books, found that its reserves for a particular type of policy—with which it had been having a bad claims experience, especially during the depression years—should be increased by $23,000,000. As such an increase would have made the Old Company technically insolvent under § 986 of the Insurance Code,* the Commissioner took over control of the business as statutory Conservator, put in a new management, organized the New Company as his rehabilitation agency, and turned over the assets and business to the New Company, in exchange for its capital stock and its assumption of all liabilities of the Old Company except those growing out of the type of insurance that had caused the trouble—the non-cancellable accident and health policies ("non-can" policies). Those were assumed upon a scaled-down basis.

The terms on which the New Company took over the assets and business were set forth in a Rehabilitation Agree-

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*Throughout the litigation resulting from the receivership and rehabilitation proceedings, the courts have been at pains to point out that the Company's difficulties were of a temporary character, not involving true insolvency. *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal. 2d 307, 325; *Neblett* v. *Carpenter*, 305 U. S. 297, 299. See also the opinion of the trial court in *Carpenter* v. *Pacific Mut. L. Ins. Co.* (not officially reported), Superior Court, Los Angeles County, December 3, 1936, contained in the Record on Appeal in *Neblett* v. *Carpenter, supra.*

ment (App. F), which the Commissioner, after obtaining approval of the Superior Court, caused the New Company to enter into with himself as Conservator of the Old Company. Certain objecting policyholders took an appeal from the order approving the Rehabilitation Agreement. The Supreme Court of California affirmed the order, *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal. 2d 307. This Court granted certiorari and, in *Neblett* v. *Carpenter*, 305 U. S. 297, rejected the contention that the Rehabilitation Agreement deprived the policyholders of their property without due process and impaired the obligation of their contracts, upon the ground that the policyholders were not bound to accept the New Company's policies but were afforded the alternative of recovering from the Old Company for breach of contract.

The Rehabilitation Agreement made provision for restoring gradually to the holders of non-can policies the benefits thereof which the New Company did not assume. The source of funds for such restoration was to be the earnings of the Departments other than the Participating Life Department.* Earnings flowing into the general corporate funds were to be put in a Special Fund for restoration of non-can benefits, in "such amounts as [the]

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*Under the Rehabilitation Agreement, the Participating Department of the New Company was to be set up as a separate entity, as if it were a separate mutual life insurance company, and its surplus was to be held solely for the benefit of the participating policyholders, except for a rather elaborate provision for an annual contribution by the Participating Life Department toward the payment of non-can liabilities, of 10% of profits derived from participating policies written by the Old Company and reinsured by the New. Inasmuch as the Price Determination Committee later found that the contributions of the Participating Department to the Special Fund for non-can restorations would be so small that they could be disregarded, we omit further reference to those provisions of the Rehabilitation Agreement. (Ex. 28, p. 11)

Board of Directors shall determine to be not reasonably required for the reasonable, proper and profitable conduct of the operations of the New Company as a going concern", subject to the right of the Insurance Commissioner to require transfer of additional amounts to the Special Fund if he thought they were available under the quoted test. (App., F 16).

Neither in the proceedings which culminated in this Court's decision, nor in any of the other litigation involving the Pacific Mutual rehabilitation,* was any issue raised or litigated with respect to the mutualization provisions of the Rehabilitation Plan, next to be discussed.

3. *Mutualization provisions of Rehabilitation Agreement*

The Rehabilitation Agreement, in effect, postponed the operation of the mutualization statutes to the Pacific Mutual situation for ten years, but provided machinery by which mutualization proceedings might be instituted in the future. The machinery might be set in motion at any time from July 1, 1946, to December 31, 1947, by requests from 10% of the holders of *participating* policies that the New Company be mutualized, in which event an Appointing Committee would be constituted and would in turn designate a Price Determination Committee of 3 to 5 persons "skilled in matters of insurance company valuation". The Price Determination Committee (the "PDC") would then (1) determine whether mutualization "can then be practicably accomplished having regard to the interests of all persons interested in the new company," and (2) if, in the opinion of a majority of the PDC, mutualization was "then

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**Carpenter* v. *Pacific Mut. L. Ins. Co.*, 13 Cal. 2d 306; *Neblett* v. *Pacific Mut. L. Ins. Co.*, 22 Cal. 2d 393; *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 23 Cal. 2d 94; *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 23 Cal. 2d 334; *Sanborn* v. *Pacific Mut. L. Ins. Co.*, 42 Cal. App. 2d 99; and *Garrison* v. *Pacific Mut. L. Ins. Co.*, 83 Cal. App. 2d 1.

practicable", it would go on to "determine the proper price to be paid upon such mutualization and appropriate terms of payment thereof." (App., F 24-26).

By the terms of the Rehabilitation Agreement, the Commissioner restricted his right as Conservator to sell or otherwise dispose of the New Company's stock, except subject to the "option to mutualize", and agreed that, if a plan of mutualization should be proposed in the manner provided for in the Agreement, he and his successors in interest as holders of the New Company's stock would consent to it (App., F 27). However, the Commissioner imposed two conditions on the covenants and consents that he gave in the Rehabilitation Agreement, (a) that if any of the provisions relating to mutualization "should be contrary to law or illegal or void" (App., F 31), that provision would be deemed separable, and its invalidity would not effect the validity of the other provisions; and (b) that his undertakings as Conservator (*e.g.*, his advance consent to a mutualization plan) were made only in his capacity as Conservator or Liquidator, "and to such extent as he had authority to make, and the Conservator makes no warranty of his authority to make the same" (App., F 34).

4. *Mutualization proceedings*

In 1946 the New Company, having obtained the necessary requests from participating policyholders, commenced proceedings for mutualization. A Price Determination Committee (the "PDC") was appointed, and commenced its task early in 1947. It employed a Chief Actuary, Mr. Christman, and a staff, who under instructions of the PDC undertook to make a valuation of the capital stock of the New Company as of December 31, 1948.

The four members of the PDC were distinguished and honorable gentlemen; but it would be hard to maintain on the basis of their connections and ties of interest—and impossible to maintain, we contend, in the face of what they did—that they were impartial, or unsympathetic to the desire of the New Company's management to mutualize, get rid of its stockholding interest and become self-perpetuating. Mr. McAndless, the Chairman, was president of a stock insurance company which enjoyed friendly relations with the New Company and was one of its reinsurers. The two other insurance men on the PDC were executives of large mutual companies; and the fourth member was a partner of a firm that sold securities and numbered the New Company among its important customers (Clk. Tr. 18-19, 66-68).

On November 9, 1949, the actuaries completed their report. They found that the 1948 value of the capital stock of the New Company was $2,614,000 on one assumption as to the future earnings of the Company on its investments (2.9%) and $3,395,000 on a slightly different assumption as to earnings on investments (3.0%). (Ex. 28, p. 2).

On April 4, 1950, the PDC submitted its Report, appending thereto a fully developed Plan of Mutualization. Appendix G hereto contains the PDC report and those portions of the Plan to which we have need to refer.

5. *Finding as to practicability of mutualization*

The PDC in its report made the necessary *jurisdictional* finding that mutualization could *"then* be practicably accomplished"; but it wrote a plan that could not be "practicably accomplished", according to the PDC's own estimates, before 1971—that being the earliest year when restoration of benefits under the non-can policies would

have been completed. The PDC found that the purchase price could not be paid until the non-can benefits had been fully restored, and could not be paid even then unless the Company's financial position was such that, after payment of the purchase price, it would "remain in possession of requisite and satisfactory reserves and in safe and efficient financial condition." (App., G 2).

Visualizing the possibility that non-can restorations might take longer than estimated, or that it might be some years after restoration before the New Company would be in a financial position to buy its stock, the PDC in its report decreed that "the time within which mutualization may be effected [under the Plan] is hereby extended to and including December 31, 1983." (App., G 3).

In short, the PDC made the jurisdictional finding that mutualization could *practicably* be *accomplished* as of December 31, 1948, but extended the time within which mutualization might *actually* be *effected* by 35 years from that date; and it then went on to provide that, if it had not been accomplished by that date, "this Mutualization Plan shall be considered to have failed". (App., G 15).

According to Webster, "Accomplished" means "completed; effected; * * *"

6. *Fixing of the Purchase Price*

Not only did the PDC make a finding, plainly contrary to fact, that mutualization could be practicably accomplished as of December 31, 1948, but it fixed a price that was based upon an imaginary mutualization on that date. The base price to be paid was fixed at $3,000,000, found to be the value of the stock on that date. Interest, at the rate carried by the longest term government bonds (2½% as of 1949) was to be payable on the price from December 31, 1948,

if, as and when the price should ever become payable; and the third element of the price formula was a contingent addition to the price of $250,000 per year (without interest) for each full year (if any) by which non-can benefits shall have been fully restored prior to December 31, 1973. (App., G 5-6).

The arithmetical basis for the findings of value by the actuaries and the PDC is set forth on pp. 9-10 of Exhibit 28, the two sections of which are interleaved between this page and the next page, labeled Chart I and Chart II. The actuaries performed a monumental series of arithmetical calculations, based upon assumptions given them by the PDC—including assumptions with respect to the future operation or influence of each of the 18 variables listed in the margin.*

Using those assumptions, the actuaries computed—for the years 1949 to 2000—what the "pattern" of earnings of the New Company would probably be and how much of them would be available for application to non-can restoration, from the three sources of earnings shown in the heading of the Charts.

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*Interest rates prevailing from time to time in the money markets; rates at which policyholders would allow their policies to lapse; rates of expenses of the business; probable volume of life insurance written on a non-participating basis; volume of business of the Accident and Health Department; probable rates of disability; rates at which the proceeds of the policies would be left with the Company on option; profits on group insurance; rates on future claims on the non-can policies; persistency of non-can benefits admitted to claim; rates of expenses in administering non-can business; probable or optimum rate of restoration of non-can benefits; average cost of non-can claims once submitted; mortality rates; reserve standards for existing and future life insurance; reserve standards for annuities and disability benefits; amount to be added to surplus to maintain relationship between surplus and volume of business, assets and liabilities; discount rate to be used in estimating value of future earnings on present value basis. (Tr. 249-253, 150-152, 380, 389, and 506.)

CHART I

PACIFIC MUTUAL ESTIMATED FUTURE EARNINGS AVAILABLE TO MEET RESTORATION COST OF $22,000,000

($ M)

Year	Source			Total—Basis A		Provision for .1% per Annum Lower Interest	Total—Basis B	
	Non-participating Life	Cancellable Accident & Health	Earnings on Capital & Surplus 12/31/48	Undiscounted	Discounted @3% to 12/31/48		Undiscounted	Discounted @3% to 12/31/48
1949	138	387	347	872	862	95	777	770
50	—98	401	347	650	626	100	550	531
51	—47	412	347	712	665	106	606	568
52	36	422	347	805	730	111	694	631
1953	40	431	347	818	719	117	701	619
1954	127	438	347	912	779	122	790	677
55	172	445	347	964	799	127	837	696
56	256	452	347	1055	848	133	922	743
57	348	456	347	1151	898	138	1013	792
1958	413	460	347	1220	924	143	1077	817
1959	496	465	347	1308	962	151	1157	853
60	602	468	347	1417	1011	158	1259	900
61	685	471	347	1503	1041	165	1338	929
62	775	474	347	1596	1073	172	1424	959
1963	840	477	347	1664	1086	179	1485	971
1964	917	478	347	1742	1105	184	1558	990
65	1001	480	347	1828	1125	189	1639	1011
66	1064	481	347	1892	1130	194	1698	1016
67	1137	483	347	1967	1141	200	1767	1027
1968	1178	484	347	2009	1131	205	1804	1018
1969	1223	485	347	2055	1123	210	1845	1010
70	1283	486	347	2116	1122	215	1901	1010
71	1340	487	347	2137 37*	1100	220	1954	1008
72	1400	488	347	2235		224	2011	1007
1973	1452	489	347	2288		228	2060 944	1002
1974	1774	509	347	2630		232	1454*	445

Total of Discounted Earnings for Period Needed for Restoration

Restoration on Basis A; Completed During 1971	22000	
Restoration on Basis B; Completed During 1974		22000

*Earnings during final year of restoration split into two parts. The amount above the line is that required to complete restoration. The amount on the line is available for stockholders.

CHART II

PACIFIC MUTUAL ESTIMATED FUTURE EARNINGS AVAILABLE FOR STOCKHOLDERS FOLLOWING RESTORATION.

($ M)

Year	Source			Total—Basis A			Total—Basis B	
	Non-participating Life	Cancellable Accident & Health	Earnings on Capital & Surplus 12/31/48	Undiscounted	Discounted @10% to 12/31/48	Provision for .1% per Annum Lower Interest	Undiscounted	Discounted @10% to 12/31/48
				2137	4			
1971	1340	487	347	37*				
72	1400	488	347	2235	240			
1973	1452	489	347	2288	223			
							944	
1974	1774	509	347	2630	232	232	1454*	129
75	1851	510	347	2708	216	236	2472	198
76	1915	510	347	2772	202	239	2533	185
77	1980	510	347	2837	187	242	2595	172
1978	2060	510	347	2917	175	244	2673	161
1979	2111	510	347	2968	162	246	2722	149
80	2166	510	347	3023	150	248	2775	138
81	2208	510	347	3065	138	250	2815	127
82	2247	510	347	3104	127	251	2853	117
1983	2280	510	347	3137	117	252	2885	108
1984	2315	510	347	3172	107	253	2919	99
85	2341	510	347	3198	99	254	2944	91
86	2363	510	347	3220	90	255	2965	83
87	2383	510	347	3240	82	256	2984	76
1988	2401	510	347	3258	76	256	3002	70
1989	2421	510	347	3278	69	257	3021	64
90	2428	510	347	3285	63	257	3028	58
91	2444	510	347	3301	57	258	3043	53
92	2459	510	347	3316	52	258	3058	48
1993	2466	510	347	3323	48	259	3064	44
1994	2470	510	347	3327	43	259	3068	40
95	2478	510	347	3335	40	259	3076	37
96	2483	510	347	3340	36	260	3080	33
97	2484	510	347	3341	32	260	3081	30
1998	2489	510	347	3346	30	260	3086	28
1999	2489	510	347	3346	27	260	3086	25
2000	2494	510	347	3351	271	260	3091	251
To Perpetuity								
Total of Discounted Earnings After Restoration Available for Stockholders					3395			2614

*Earnings during final year of restoration split into two parts. The amount above the line is that required to complete restoration. The amount on the line is available for stockholders.

The actuaries also estimated how much the future non-can claims from year to year would be and, again using assumptions as to future conditions given to them by the Chairman of the PDC, ascertained that the amounts needed for payment of all existing and estimated future non-can claims, discounted to 1948 at a compound interest rate of 3%, came to $22,000,000. They then took their estimates of earnings from 1949 on, and discounted them year by year to 1948 values at the same 3% compound rate, continuing that process until they reached the point where the discounted value of the aggregate earnings reached $22,000,000—the estimated 1948 value of the non-can liabilities. (Ex. 28, p. 8).

That point was reached in 1971 or 1974, depending upon alternative assumptions as to how much return the New Company would earn on its investments—whether 3% or 2.9%. The earnings thus equated with the non-can liabilities were not all the earnings for the years from 1949 to 1971 or 1974, but only those that were "available" for that purpose under a formula which will be described, and which allowed for annual additions to the corporate surplus.

So they said in effect: All the earnings of the Company, otherwise available for dividends to stockholders, will be needed to restore non-can benefits up to 1971 or 1974, and so those earnings will contribute nothing to the value of the stock. Hence they must be left out of account in determining the 1948 value of the stock. That value must be determined by finding out how much the stream of earnings from 1971 or 1974 would be worth to a person purchasing the stock on the fictitious sale date of December 31, 1948.

Accordingly, the actuaries proceeded to find the 1948 value of the estimated stream of earnings from 1971 to 2000 and from 1974 to 2000. They ~~discontinued~~ discounted each year's earnings estimate back to 1948 on a compound interest basis

(but this time at 10%, instead of 3% as for the earlier years). They added approximately $250,000 to the figure for 2000 A. D., to allow for the value of the earnings from the year 2001 to the end of time; and they came out with the two figures given above, which average $3,000,000; and the PDC fixed that figure as the base price.

The actuaries' Report well says of their own estimates:

> "These estimates are, of course, subject to great uncertainty. They are the result of an extensive series of calculations which have been carefully carried out, but which involve assumptions as to happenings in the distant future which may or may not be realized" (Ex. 28, p. 8).

The PDC's computation of the value of the stockholders' equity in terms of the stream of earnings (using the average of its two figures for the years after 1971 or 1974) was in simple terms as follows:

Value of stream of earnings, 1949 to 1971 or 1974, available for non-can restorations	$22,000,000
Value of stream of earnings, 1971 or 1974 to perpetuity, available to stockholders.	3,000,000
Total value	$25,000,000
Deduct estimated cost of non-can restorations	22,000,000
Value of stockholders' equity as of December 31, 1948	$ 3,000,000

7. *Provisions for payment of purchase price*

The PDC, having found that the New Company would not be able to pay for its stock until a distant future date, made the payment, at whatever date, subject to three con-

ditions: (a) that non-can benefits had been fully restored, (b) that the New Company's capital and surplus, plus a Special Fund to be created out of profits of the Participating Department, should equal or exceed the purchase price with interest, and (c) that the surplus (after paying for the stock) would still be at least the sum of (i) 4% of the admitted assets of the New Company plus (ii) 25% of premiums collected during the previous year on all group insurance written on a one-year term basis and (iii) 25% of premiums collected during the previous year on all accident and health insurance. (App., G 8).

The drastic character of the third condition may be shown from the New Company's published figures* for 1954:

4% of admitted assets ($493,000,000)	$19,720,000
25% of 1954 group insurance premiums ($5,960,000)	1,490,000
25% of 1954 accident and health premiums ($27,000,000)	6,750,000
Total	$27,960,000

Thus, on the basis of the financial situation of the Company at the end of 1954, it will not come under any obligation to buy its stock pursuant to the Plan of Mutualization unless and until, *after paying the purchase price,* it will have not less than $27,960,000 of surplus left. It will not have to buy its stock for $3,000,000 plus interest, unless and until the book value of the stock is 10 times the price, plus interest.

8. *Proceedings Below*

The mutualization proceedings were had, and the order of the Commissioner was made, under §§ 11525-27 of the

*1955 Best's Life Insurance Reports 970.

California Insurance Code. Section 11525 authorizes a solvent domestic insurer to mutualize and to provide and carry out a plan for that purpose. Section 11526 provides that the plan must be (a) adopted by a majority of the directors, (b) approved by the holders of at least a majority of the outstanding shares, (c) submitted to the Commissioner and approved by him in writing, and (d) approved by a majority of the policyholders for whose benefit the stock is to be acquired. It becomes effective when filed in the office of the Insurance Commissioner after the foregoing requirements have been met. All steps except the last one have been taken. Approval of stockholders was given by the Voting Trustees to whom the Commissioner as Conservator had transferred the stock and by the Conservator himself.* Neither the Old Company nor its stockholders, the beneficial owners of the stock, were given any voice in formulating, or any right to vote on, the Mutualization Plan. Section 11527 provides (App., E 11):

> "The commissioner shall examine the plan submitted to him under the provisions of subdivision (c) of section 11526. He shall not approve such plan unless in his opinion the rights and interests of the insurer, its policyholders and shareholders are protected nor unless he is satisfied that the plan will be fair and equitable in its operation."

The Commissioner held a hearing and heard testimony and argument in support of and in opposition to the Plan from August 1 to 18, 1950, and rendered his decision on September 22, 1950. The New Company and other interested parties, including the appellant stockholders, appeared in the proceeding. Two members of the PDC—the Chair-

*In giving their consent, the Voting Trustees expressly stipulated that they had not considered the merits of the Plan (Ex. 21, p. 4).

man and the banker member—and Mr. Christman, the chief actuary, testified in support of the PDC's finding of value for the New Company's stock, and were cross-examined by appellants' counsel.

The Commissioner in his opinion made reference to three bases of valuation of the New Company's stock which had been mentioned in the testimony—two of which the PDC itself had rejected—and said there was "abundant evidence" to support the PDC's findings; that they had arrived at the $3,000,000 price "in the exercise of their judgment"; and, in effect, that he accepted their judgment (App., D 17-18). The opinion clearly reveals that the Commissioner did not look beyond the PDC's explanation of their valuation of the New Company's stock. He did not avail himself of the facts and figures with which the facilities of his office could have provided him. In essence, he followed the "expert" judgment of the Committee in approving the Plan.

The Commissioner held that the Old Company was foreclosed from objecting to the Plan because it was bound by the 1936 consent given by the Conservator. He did not *say* that the stockholders were similarly foreclosed, but that was the effect of his decision. His conclusory finding was (App., D 24):

> "IT IS HEREBY FOUND AS A FACT that the rights and interests of the New Company, its policyholders, and the holder (sic) of its shares are protected under the terms of the plan hereinabove referred to, and that the plan will be fair and equitable in its operation."

Appellants filed their petition for mandate in the Superior Court, and raised the constitutional questions now before this Court as follows (Clk. Tr. 22):

> "Said order of Insurance Commissioner . . . was and is null and void, and of no effect, and was arbitrary and unreasonable. . . . Said findings of the Insurance Commissioner are . . . contrary to the weight of the evidence, and are not supported by substantial evidence adduced at said hearing, or otherwise. Said Findings and Order of said Commissioner deprive Petitioners . . . of property without due process of law, contrary to . . . the Fourteenth Amendment to the Constitution of the United States. In this respect Petitioners here refer to their Points of Error hereto attached and presented with this petition."

In their Points of Error, appellants objected to the contingent, long-delayed and possibly illusory character of the obligation to buy the stock, the vague, hypothetical and uncertain bases for the PDC's valuation of the stock, and the failure of the Insurance Commissioner to make an independent examination of the fair value of the stock (Clk. Tr. 28, 30, 31, 32, 32-33). The Superior Court overruled appellants' contentions, and said (App., C 33-34):

> "PDC might well have approached the problems presented to it and resolved those problems differently than they did. We may not agree with their approach or with their reasoning, but we cannot say, nor could the Commissioner say, that they acted without reason, and neither the Commissioner nor this Court can substitute his or its reasoning for that of the Committee."

The Superior Court invoked the rule of substantial evidence to support the Commissioner's order, but did not find that the Commissioner himself had considered the evidence and arrived at a conclusion based upon the evidence

before him. What it found was that PDC had reached a conclusion based on substantial evidence *before it.* The Court held that it was not the Commissioner's duty "to look behind the report of the Price Determination Committee and make an independent determination of the value of the stock and the fairness of the price" (App., C 31), that the Commissioner was "bound" to find that the plan was fair to the appellants "unless the evidence disclosed that the Price Determination Committee acted arbitrarily" (App., C 31), and that the Commissioner could not say that the PDC "acted without reason" and could not "substitute his . . . reasoning for that of the committee" (App., C 34).

The Court plainly indicated that, if he had had to decide on the fairness of the Plan upon the evidence before him, he would not have approved it. He said (as quoted in Judge Carter's dissent below, App., A 65; emphasis is Judge Carter's):

> " . . . *I think it must be very evident if I had had this case decided on a new question of fact my decision might have been the opposite.* . . . It was only because I could not convince myself that it was not a rational conclusion that they acted upon that I ever decided the case the way I did. *Because I could not take the facts and arrive at the same conclusion; not by a long shot. But because I did not feel that I could substitute my opinion for the Commissioner's, that is the reason I arrived at the conclusion that I did.*"

In the District Court of Appeal, appellants again raised the constitutional questions. That Court also purported to apply the substantial evidence rule but, like the Superior Court, went on to hold that it was for the PDC to make the determination of value. It said, in response to the contention that the Insurance Commissioner had not made a

determination of value required by his statutory duties (App., B 28):

> "One answer to this is that the power and duty to determine the value and price of the stock was lodged *in the Price Determination Committee and not in the Insurance Commissioner,* by the Rehabilitation and Reinsurance Agreement, and *this committee* was thereby empowered to determine the price to be paid for the stock on any reasonable basis. The determination of value was made by the Committee. . . and we are unable to hold, from the record, that the conclusion *it* arrived at was unreasonable." (Emphasis ours)

Thus the Court wrote out of § 11527 of the Insurance Code what on its face appears to be a requirement that the Commissioner must make an independent determination of the fairness of any voluntary mutualization plan; and by doing so, we contend, the Court rendered the statute unconstitutional. The District Court of Appeal also passed specifically on appellants' claim with respect to substantive due process (App., B 34). It noted:

> "Another point raised by the appellants is that they have been deprived of substantive due process because the stock of the New Company was valued as of the present, that the time of payment was fixed long in the future, payment was conditional, there was no provision for reasonable interest, and the price paid was grossly inadequate."

Those contentions were disposed of by a holding that "the commissioner's approval of the plan of mutualization did not have the effect of taking appellants' property, since it was nothing more or less than a permit. . . ." (App., B 34).

Appellants raised the questions here presented in the California Supreme Court (Pet. H. 71-84). Their conten-

tions as to substantive and procedural due process were rejected. The Court said (App., A 14):

> "The approval of the mutualization plan by the Commissioner did not involve any deprivation of property rights or vested rights . . . the function of the superior court was to determine whether the action taken by the commissioner was arbitrary or constituted an abuse of discretion, and in upholding the action of the commissioner, it properly refused to conduct a trial de novo."

Justice Carter's dissenting opinion sets out at length the reason for his conclusion that, under the decisions of this Court, appellants were denied due process of law under Amendment XIV. (App., A 61-66).

Appellants' Petition for Rehearing in the California Supreme Court was based upon the Federal constitutional questions above specified. (Pet. Reh. 27-42).

9. *Res Judicata*

The courts below held, in substance, that the Rehabilitation Agreement was binding upon the Old Company and that the procedure for bringing about mutualization was a matter of *res judicata*. The issue of *res judicata* is discussed at length in the opinions of the majority and dissenting judges in the California Supreme Court (App., A 8-12, 13, 19-21, 47-56). By invoking *res judicata,* the courts below were able to avoid a number of troublesome issues; but they did not, we submit, avoid the issue of confiscation, or the issue of a fair hearing and adequate judicial review, which are presented in the argument to follow. If the requirements laid down by this Court in *Case* v. *Los Angeles Lumber Co.,* 308 U. S. 106, have a constitu-

tional basis, then the application of *res judicata* by the courts below resulted in, or contributed to, a denial of due process of law.

Substantial constitutional questions are raised on this appeal

Substantive due process

The order of the Commissioner—which was an exercise of delegated legislative power,* and therefore a statute within the meaning of § 1257(2) of the Judicial Code—is unconstitutional because it provides for the taking of appellants' property at a price that is plainly confiscatory. The Plan of Mutualization derived its compulsory character from the Commissioner's order; hence the property of appellants has been taken by the State itself. *Doty* v. *Love*, 295 U. S. 64; *Union Dry Goods Co.* v. *Georgia P. S. Corp.*, 248 U. S. 372; *Eubank* v. *Richmond*, 226 U. S. 137.

1. It was plainly a violation of due process to provide for the taking of appellants' property at a remote future date upon payment of a price equal to a value determined as of a date many years before. See *Olson* v. *United States*, 292 U. S. 246, 254-55.

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*Mutualization of an insurance company is a legislative function, an exercise of the reserved power of the legislature to alter, amend and repeal corporate charters; and the order of the Insurance Commissioner approving the particular plan of mutualization was legislative in character. *Lord* v. *Equitable Life Assurance Society*, 194 N. Y. 212. While, to perform his delegated function to pass on the fairness of the Plan, the Commissioner had to act quasi-judicially, his order had a legislative effect and was a legislative act. *Belden* v. *Union Central Life Insurance Co.*, 143 Ohio St. 329; *In re Prudential Insurance Company*, 82 N. J. Eq. 335; *Rippel* v. *Prudential Insurance Company*, 85 N. J. L. 395; *Application of Prudential Insurance Company*, 132 N. J. Eq. 170.

Mutualization is a form of corporate reorganization; and the courts in reorganization proceedings must determine values as of the time when interests are taken or adjusted. This Court has said: "Valuation on the basis of a going concern necessarily has primary relationship to value as of the time the shareholders' surrender becomes effective, not as of some earlier, remote period or one long afterward." *SEC* v. *Central-Illinois Corp.*, 338 U. S. 96, 138, 139. *Cf. St. Joe Paper Co.* v. *Atl. Coast Line R. R.*, 347 U. S. 298, 300; *In re Equitable Office Bldg. Corp.*, 96 L. Ed. 1386, not officially reported; *Ecker* v. *Western Pacific R. R.*, 318 U. S. 448, 462; *Matter of Globe & Rutgers Ins. Co.*, 148 Misc. 497, 501.

The utterly confiscatory character of the PDC's device of fixing values as of 1948, when payment is not to be made until some remote future date, may be seen from its own figures. The PDC valued future earnings available to stockholders (after 1971 or 1974) on a 10% compound discount basis. If we follow that method, and discount the estimated earnings up to the year 2000, but to their "present value" as of 1974 instead of 1948, we get a 1974 valuation of those earnings of approximately $27,700,000. Thus if the stock is bought and the price paid in 1974, the situation will be as follows:

Value of stockholders' equity in 1974, based on PDC's estimates of earnings from 1974 to perpetuity		$27,700,000
Purchase price:		
1948 value	$3,000,000	
Interest at 2½%, 1949 to 1974	1,875,000	
Total price		4,875,000
Excess of estimated value of stockholders' equity over price to be paid for it at the time of purchase		$22,825,000

Thus the owners of the equity will be paid a little over 20% of the value of their property at the time it is taken —not the value asserted by us, but the value based on the PDC's own figures. Under all the authorities, they are entitled to the value at the time of purchase.

The New Company will not become obligated to purchase and pay for its stock until a number of conditions have been fulfilled, one of which is that the non-can restorations—estimated to require a capital fund of $22,000,000, as of 1948—shall have been paid off. Those liabilities will be restored out of earnings available for the purpose over the years; and meanwhile, according to the PDC's estimates, the business, the assets and the surplus of the New Company will gradually increase, so that the value of the equity—before non-can deductions—will never be less than $25,000,000. But when the non-cans are paid off, the $22,000,000 deducted from the 1948 equity value will have dis-

appeared; and the net value of the stockholders equity will be at least $25,000,000.

So the proposal that the New Company has made to the Old Company and its stockholders amounts to this: Your property was worth $3,000,000 on December 31, 1948. When it has increased in value to not less than $25,000,000 (and provided other conditions are satisfied), we will buy it for $3,000,000 plus interest.

In *Matter of New York Title & Mortgage Co.*, 171 Misc. 489, the New York courts, on objection of stockholders, disapproved a similar but infinitely less drastic proposal of the Superintendent of Insurance to fix the price for sale of the company's assets, where payment would be delayed pending fulfillment of certain conditions. The Court held that the price would have to be approved at the time when the sale was actually made, pointing out that there might be an increase in the value of the assets before that time, and that the stockholders were entitled to the benefit of such an increase if it occurred. That decision is only an application of the generally accepted principle that when property is taken it must be paid for at the value at the time of the taking. *Monongahela Navigation Co.* v. *United States*, 148 U. S. 312; *Olson* v. *United States*, *supra*.

2. When a public authority takes property, due process requires that it make adequate provision for *certain* and *not unreasonably delayed* payment of just compensation to the owner. *Cherokee Nation* v. *Kansas R. R.*, 135 U. S. 641; *Sweet* v. *Rechel*, 159 U. S. 380; *Backus* v. *Fort Street Union Depot Co.*, 169 U. S. 568. Where, as in our case, the State is taking property from one private group and giving it to another, the application of that standard seems

more compelling than in the case of condemnation, where public purposes are being served. See *Thompson* v. *Consolidated Gas Co.*, 300 U. S. 55, 79-80.

In this case, the equitable ownership of the stock of the New Company has been subjected to a 35-year option; and for that option *no compensation whatsoever* has been paid. The Old Company and its stockholders have been deprived of the ordinary right of a property owner to determine when he will sell and for how much—a right that is "property" within the protection of Amendment XIV. See *Old Dearborn Co.* v. *Seagram Corp.*, 299 U. S. 183, 192; *Buchanan* v. *Warley*, 245 U. S. 60, 73.

The stockholders of the Old Company have been deprived of the right to raise money to pay off the non-cans and redeem their equity, or to get back their property when the non-cans shall have been paid off (App., F 29-30). Control of the stock of the New Company will be turned over to Voting Trustees, whose status and duties have been meticulously phrased to exclude any possible fiduciary obligation or relation to the Old Company or its stockholders (App., G 16); and thus appellants will be deprived of the benefits of the trust (with the Conservator as trustee) which the statute created for the protection of all interests, including theirs.* (App., C 22-23, 25).

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*The stockholders have also been deprived of one of the most important safeguards provided for them in the Rehabilitation Agreement—that the New Company must follow a policy of writing at least 50% of its life insurance as non-participating insurance. The stockholders derive no benefit from the participating insurance, since the Rehabilitation Agreement set up the Participating Department as if it were a separate mutual company. Therefore the New Company could completely defeat the interests of stockholders, postpone the date of purchase of the stock and keep the purchase price down by writing more participating and less non-participating insurance. The provisions of the Plan of Mutualization affecting this point are so outrageously watered down that the stockholders are without practically any protection against such a course by the New Company (App., G 12-13).

Preserving the fiction that mutualization was being accomplished as of December 31, 1948, the PDC even deprived the stockholders of the value of their interest in those earnings prior to 1974 which will be added to surplus from year to year. While not the most significant in terms of value, this was perhaps the PDC's most extraordinary departure from accepted principles governing the valuation of the stockholders' equity in a corporation.

In arriving at its earnings figures for the years 1949 to 1974, the PDC *deducted* $190,000 per year to be added to surplus, on the theory that, as the business grew, the surplus should be allowed to grow in proportion (Ex. 28, p. 12; Tr. 545-47). It also *excluded* from earnings all money that might be earned on those additions to surplus. The balance of annual earnings was what it found to be available for non-can restorations.

It then valued at zero the stockholders' equity in the "stream of earnings" to 1971 or 1974, available to restore non-cans, ignoring the stockholders' interest in the gradually increasing surplus. The PDC seems to have labored under the curious misconception that, if earnings are retained and ploughed back into the business, they do not add anything to the value of the stockholders' interest. What the Committee did, in excluding the accumulating surplus as an element of value, is as absurd as it would be to appraise the stockholders' equity in U. S. Steel without taking account of the billion dollar surplus which that corporation has built up.

On the PDC's figures, the increase in the corporate surplus to 1974 was to be $7,260,000 (Tr. 693-94). If the PDC had taken that factor into account, and discounted it back to 1948 as it did the other figures for the 1949-1974 period, it would have found the stock of the New Company to have a value, as of December 31, 1948, of about

$3,500,000 more than it actually found. Its computation of price, as shown above (p. 14) would have to be revised as follows:

Value of stream of earnings, 1949 to 1971 or 1974, available for non-can restorations	$22,000,000
Value of stream of earnings thereafter, to perpetuity, available to stockholders (average figure)	3,000,000
Value of stream of earnings, 1949 to 1974, not available for non-can restorations but added to corporate surplus and stockholders' equity	3,500,000
Total	$28,500,000
Deduct cost of non-can restorations	22,000,000
Value of stockholders' equity as of December 31, 1948	$ 6,500,000

When compared with the other outrageous departures from proper and constitutional methods of valuation which the PDC made, this is a minor one. Yet it alone produced an undervaluation of $3,500,000—on the PDC's own figures, and even conceding that it will be proper to buy the stock in 1974 at its 1948 value.

In considering the rights and property interests of which the stockholders have been deprived, pending either the consummation of the Plan or the return of their stock if the Plan fails, it must be noted that, because of the third condition imposed upon the obligation to pay—that relating to the amount of surplus that the New Company must have before it will be obligated to pay*— there may be a long interval between the restoration of non-can benefits and

*Supra, p. 15.

payment of the price. This point is particularly significant in relation to the $250,000 price adjustment provision, and it is discussed in more detail under that heading, but it also deserves mention here.

It could happen that the non-can restorations would be completed as early as 1963; and yet it might be 1983 before the New Company would have the large surplus which it must have before it is obligated to buy—an interval of 20 years. During that time, according to the estimates of the PDC, aggregate earnings will approximate $50,000,000; and they would be available for dividends on the stock, the non-cans having been paid off. Yet the Plan makes no provision for payment of any dividends on the stock; it does not contain a single reference to any rights of the Old Company or its stockholders. As it would clearly be contrary to the interests of the management of the New Company to pay dividends during the 20-year interval assumed, and as they would have no obligation to do so, the stockholders in the case supposed would be deprived of a return on their investment for 20 years, though the earnings would be (on the PDC figures) ample to give them a handsome return.

4. The provisions of the Plan of Mutualization for interest on the purchase price are inadequate and confiscatory in three respects, (a) the rate fixed, (b) the time of payment and (c) its contingent character.

The purpose of interest, where property is taken and payment delayed, is to give the owner "such addition as will produce the full equivalent of that value paid contemporaneously with the taking." See *Seaboard Air Line R. R.* v. *United States*, 261 U. S. 299, 306; *Jacobs* v. *United States*, 290 U. S. 13; *Phelps* v. *United States*, 274 U. S. 341. That means interest at compensatory rates.

Simple interest at 2½%, even if payable currently, would have been inadequate. See *Louisville Bank* v. *Radford*, 295 U. S. 555, 591, 592. Payable at the end of 25 years or longer, 2½% interest is equivalent to not more than 1.99% payable annually—obviously a confiscatory rate.

The PDC defended the interest provisions on the ground that they called for as much interest as the New Company could afford to pay (Tr. 157). There is no better example of the bias of the PDC. If the New Company was not able to pay a fair and compensatory rate of interest on the postponed payment of any price that might be fixed, then clearly, and apart from all other factors, mutualization was not *then practicable*. But, the PDC, having found mutualization practicable, resolved the problem by fixing an interest rate far below the compensatory level.

5. The provision of the Mutualization Plan for upward adjustments of price was also grossly confiscatory. The Chairman of the PDC explained that provision as follows:

> "We reasoned that if profits were higher or restoration costs were lower than anticipated, restoration would be completed that much sooner, and the profits for stockholders interest would then accrue not from 1973 but from some earlier date. We found by calculation that if we drew the line one year earlier, two years earlier, etc., discounting the residual earnings in the same way as before, we would increase the price by something approaching $250,000 for each yearly step. Our Report provides for such an addition to the price, that is, $250,000 for each full year by which the completion of restoration antedates the end of 1973, with interest from the date of restoration." (Tr. 155)

Thus, by taking its estimates of pre-1974 earnings (which exceeded two million dollars for every year from 1968 on) and discounting those earnings back to 1948 at 10% compounded, the PDC got a rough figure of $250,000 per year for the years that it thought might be involved in a price adjustment. This time, however, for some unfathomable reason, interest was not to be paid on the additional element of price from December 31, 1948, but only from the date when non-can benefits had been restored. If the $250,000 per year price adjustment were otherwise fair and reasonable, it would be confiscatory because of the interest provision alone. But it is wholly unjustifiable apart from the disallowance of interest, and is calculated to produce a windfall for the future mutualized company. It gives the owners of the equity $250,000 for each annual sum of over $2,000,000 which they contribute to the New Company, over and above what the PDC estimated they would contribute.

Let us suppose that the restoration of non-cans is greatly accelerated, and is completed in 1963. There will then be 10 years for which a price adjustment has to be made, and the price of the New Company's stock will be increased by $2,500,000. The earnings for those 10 years, upon the lower of the PDC's two estimates, will aggregate $18,237,000. The Plan of Mutualization proposes, therefore, that, for $18,237,000 of increased assets that the equity owners contribute to the New Company, they will be paid $2,500,000, and the balance of $15,737,000 will be retained as a windfall for the future mutualized company.*

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*These figures could be made more startling by taking into account the accumulated surplus which is *counted out* in valuing the stockholders' equity.

The $250,000 price adjustment provision is particularly shocking when it is recalled that restoration of non-can benefits may occur many years before the New Company becomes obligated to buy the stock and pay the purchase price. In our supposed case, where restoration of non-can benefits is completed in 1963, the Company might not be in a position to pay the price until 1983. In each of the intervening years, on the Committee's own figures, the New Company would be appropriating to itself, and adding to its surplus, annual earnings ranging—as estimated by the Committee—from roughly $1,700,000 to $3,137,000, or total earnings of about $50,000,000. In return for that aggregate addition to surplus—plus 20 years of earnings on that surplus—the New Company under the Plan would pay an additional price of $2,500,000, with interest of $1,250,000.

If we assume that non-can restorations are only slightly accelerated, and that only the years 1971 and 1972 will be involved, the figures on a comparative basis are just as shocking. The New Company will get the benefit of estimated additions to surplus of $4,170,000, for which it will pay $500,000 plus $25,000 of interest. Then, if payment is delayed until 1983, it will have built up in the intervening years an additional surplus of over $31,000,000, according to the PDC estimates—surplus represented by securities and hard cash—for which it will pay nothing except $962,000 in the form of interest.*

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*The Plan seems to have been written to make delays in payment to the equity owners as profitable as possible for the New Company. If there is a 20 year delay, or 10 year delay, after restoration of non-cans, the Company will have to pay 2½% simple interest on the price, but it will enjoy the earnings on the equivalent amount of money at either 2.9% or 3% *compounded*, according to the PDC's estimate.

The incredible confiscation of property values which the $250,000 price adjustment provision permits is accomplished by the constitutionally unthinkable device of fixing a price to be paid in 1971 or 1983, or whatever it may be, in terms of values on December 31, 1948. Clearly the members of the PDC—however distinguished they may have been as actuaries and a banker—had not the dimmest appreciation of the rights of stockholders in a corporate reorganization.

Can there be any doubt that Judge Carter, dissenting in the court below, was justified in his statement (App., A 64), that

> "It surely must be crystal clear to everyone who can think that such an outrageous confiscation of property without due process of law has never before taken place in this state."

6. The Plan of Mutualization is confiscatory because it establishes a price for the stock which is based on speculation and guesswork, and upon assumptions having no rational basis in law or fact.

No one, however skilled in actuarial methods, can make an estimate of how much a business corporation is going to earn, in a period from 25 to 50 years in the future, which is more than a wild guess. How could anyone in 1949 make even an *educated* guess as to what interest rates would prevail, what investments insurance companies would be allowed to make, how much they might yield, at what rate policies would lapse, or what the expenses of doing business would be, in the years 1974 to 2000—to mention only a few of the variables?

Almost every assumption made by the PDC is at least debatable. For example, it assumed that mortality rates in the last quarter of the 20th Century would conform to the

past experience of Pacific Mutual—in the face of the progressive and continuing decline in mortality rates that has been going on since the beginning of the century (Tr. 150, 389).

Valuations based on estimates of factors so far in the future are almost certain to be undervaluations, when made by men with conservative habits of mind, like actuaries. With so many factors to evaluate, the effect of conservative estimation increases in geometric fashion. That the PDC was ultra-conservative in its estimates of earnings is readily demonstrable. For example, the PDC estimated that the annual amount available for non-can restorations would not reach $1,900,000 until 1967, upon the more favorable of its two assumptions. Actually, in the very first four years of the PDC's estimates—1949 to 1952—the average annual amount *applied* to non-can restorations *exceeded* $1,900,000 per year. The following compares the Committee's estimates with the actual figures (Op. Br. 127).

	Estimated	Actual
Amounts available for non-can restorations:		
From non-participating life policies	$ 29,000	$3,008,000
From accident and health policies	1,622,000	4,606,000
	$1,651,000	$7,614,000

Thus the Committee underestimated the available earnings from the sources mentioned, for 1949 to 1952 alone, by almost $6,000,000—a margin of error of some 361%.

Some of the major factors bearing on the Company's prospects, which the PDC ignored, are noted in the margin.*

Procedural due process

The order of the Commissioner approving the Plan of Mutualization is unconstitutional because, contrary to the requirements of due process, it is not supported by substantial or competent evidence, and was not based upon a fair and open hearing before an impartial tribunal; and §§ 11525-27 of the California Insurance Code are unconstitutional because, as construed and applied by the courts below, they have deprived appellants of a judicial determination of their rights and of a judicial review of an order which, they claim, confiscates their property.

1. For reasons already stated, we submit that the evidence upon which the PDC acted, and which the Commissioner accepted, was neither substantial nor reliable. "Plausible anticipations" and "flights into the realm of pure speculation" cannot be treated as evidence of value. See *Connecticut Co.* v. *Palmer,* 305 U. S. 493, 505; *Morgan* v. *United States,* 298 U. S. 468, 479-80; *West Ohio Gas Co.* v. *Comm.,* 294 U. S. 79, 82. The factors on which the PDC based its estimation of future earnings were "too contingent, too unique for guidance by experience, to permit rational

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*Among the factors that the PDC did not consider were the rapid growth of the population of the country and the expansion of industry, with a continuous increase in the number of those gainfully employed; the progressive increases in real wages and in the standard of living of low-income groups; and the phenomenal growth, both in population and industry, of the States of California and Texas, where a major part of the Company's business is done.

assessment". *United States* v. *Westinghouse,* 339 U. S. 261, 267.

2. The California Insurance Code provides two procedures for the mutualization of insurance companies. One relates to the *involuntary* mutualization of *the business of* an insolvent insurer (App., E 1). It calls for the commissioner to propose the mutualization plan, the Superior Court to pass upon it after hearing all parties and appointing appraisers to value the capital stock, and the court to make a finding of the "reasonable value of the shares, including the goodwill, if any". (App., E 7).

The *voluntary* mutualization statute (§§ 11525-27) provides for a method of mutualization exerting no compulsion on stockholders. They may vote on the plan. If it is approved by the Commissioner as fair and equitable to all concerned, the Company is authorized to buy its stock, at the price fixed by the plan, and must buy it from stockholders who are willing to sell at that price; but there is no compulsion upon any stockholders to sell his stock unless and until he wants to do so, or at any price except his own.

The voluntary mutualization statute, on its face, seems to meet all requirements of due process. It appears to encompass those instances where a stock company, in the exercise of a free choice, seeks to change to a mutual company. The court below, having found the voluntary mutualization statute to be applicable, held that the Commissioner's order was nothing more than a permit to the New Company to purchase its stock. That would have been true in the ordinary voluntary mutualization, where the stockholders have the right to disapprove any plan proposed, and to keep their stock if they wish to do so. But in this case, by treating the Commissioner as the owner of the stock, with

the right to consent to a plan of mutualization—and without reference to the wishes of stockholders of the Old Company for whom he is trustee—the California courts have permitted an *involuntary* mutualization to be carried out under the *voluntary* mutualization statute.*

By construing the order of the Commissioner as involving no more than the granting of a permit or a license, the courts below brought into play the judicial review provision of the California Code of Civil Procedure, § 1094.5(c), which imposes a test of "substantial evidence in the light of the whole record", rather than the test of the "independent judgment [of the court] on the evidence", which is applicable in cases where property is taken or vested rights affected (App., A 14-15, 57-62).

By their construction of the voluntary mutualization statutes, the California courts have deprived appellants of the independent judicial review that is required by Amendment XIV where an order of a State agency has been attacked as confiscatory. In such cases, this Court has held—even where the "taking" is for public purposes rather than for the benefit, as here, of private persons—that the State courts must review administrative action by examining and weighing the evidence, and must determine whether or not the consideration provided is below the level of just compensation. *Ohio Valley Co.* v. *Ben Avon*

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*Either the consent of the stockholders whose property is to be taken, or a judicial determination of the value of their interests, is required by every one of the 18 mutualization statutes in the United States. The statutes are collected in Parish, *The Mutualization of a Legal Reserve Stock Life Insurance Company*, 11 Proc. of Assn. of Life Insurance Counsel 475, 479-483 (1952-1953). Some of the statutes, *e.g.*, Page's Ohio Code, c. 3913, provide for the taking of stock of dissenting stockholders if a majority has approved mutualization, but provide for a judicial appraisal of value.

Borough, 253 U. S. 287, 289; *United Railways* v. *West*, 280 U. S. 234, 251. *Cf. St. Joseph Stockyards Co.* v. *United States*, 298 U. S. 38, 49-52; and see Frankfurter, J., concurring in *Alabama Comm.* v. *Southern R. R.*, 341 U. S. 341, 362.

With two exceptions, anything less than full and independent judicial determination or review of valuation is unknown in reorganization proceedings in this country. See *Kelley* v. *Everglades District*, 319 U. S. 415, 418, 419-426; *Case* v. *Los Angeles Lumber Co.*, *supra*; and *cf.*, *Penn Co.* v. *Pennsylvania*, 294 U. S. 189, 197, and *Pennsylvania* v. *Williams*, 294 U. S. 176, 182-186, where this Court scrutinized the adequacy of State statutory provisions with respect to liquidation procedures for insolvent insurance companies and building and loan associations.

This Court has sanctioned the substantial evidence form of judicial review, in reorganization proceedings involving property valuations, in only two situations so far as we are aware—the ICC railroad reorganization cases and the SEC public utility holding company simplifications. *Ecker* v. *Western Pacific R. R.*, *supra*; *RFC* v. *Denver R. R.*, 328 U. S. 463; *SEC* v. *Central-Illinois Corp.*, *supra*; *Niagara Hudson Corp.* v. *Leventritt*, 340 U. S. 336. In the *Ecker* case the Court explained its adoption of the substantial evidence rule as resting upon exceptional and compelling circumstances of public policy (318 U. S. at 468). The present case involves no comparable circumstances. The Insurance Commissioner was not dealing with a matter in the field of public regulation, and he was not concerned with striking a balance between public and private interests. What he had before him was a corporate reorganization in which there was a problem

of the just apportionment of corporate assets among private parties—stockholders, non-can policyholders and the New Company itself.

3. The hearing before the Commissioner could not be a fair and open hearing before an impartial tribunal, because the Commissioner was involved in a hopeless conflict of interests. His predecessor in office was the proponent of the Rehabilitation Agreement. As Conservator he was a statutory trustee for the Old Company and its stockholders; his advance consent, we submit, might limit but could not destroy his fiduciary obligations. He was a Voting Trustee of, and the controlling person in, the New Company (App., A 33-34; G 9-10); and he was called upon to judge the plan which the New Company had proposed, and the directors and voting trustees of the New Company had accepted, by which those conflicting interests were to be resolved. The decision below—that he could so act without judicial review, if he did not act arbitrarily or without evidence—is, we believe, without precedent.*

The California statutory provisions involved in this case were "copied, substantially from similar provisions in the New York Insurance Law". See *Carpenter* v. *Pacific Mut. L. Ins. Co., supra*, 10 Cal. 2d at 328. The limited judicial review afforded below on the issue of valuation departs from the practice observed under both the New York prototype statute and other State mutualization statutes (see footnote, p. 37), and from the standards of judicial review observed in valuation matters in corporate reorganization proceedings generally. The New York courts

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*See Davis, Administrative Law (1951) ch. 19, "Nonreviewable Action".

have exercised a close supervision over all phases of insurance company rehabilitation proceedings* for the reason, among others, that in New York, as in California, the Commissioner (Superintendent) "has been forced by the statutes defining his duties to accept the position of acting for conflicting and antagonistic interests." See *Matter of Nemerov*, 149 Misc. 797, 805-06.

Conclusion

The California courts failed to accord to appellants the judicial review that is appropriate to cases where property is taken and confiscation claimed. Had they done so, the Mutualization Plan almost certainly would have been disapproved, because the court of first instance plainly said that he would not have approved it on the evidence before him (App., A 65).

But whatever the proper scope of judicial review, the Mutualization Plan is utterly confiscatory, and should have been found to be so even on the most limited type of review.

From the figures given above, it must be clear that the New Company's stock is worth many times the price fixed for it; and our figures, except in two instances, have been the PDC's own estimates, made in 1949. Were we to take the New Company's published figures—showing earnings, additions to surplus and general business progress far beyond what the PDC estimated—it would be clear that

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*The New York State Superintendent of Insurance functions, in such proceedings, virtually as a receiver. The New York courts exercise this form of close judicial control because they consider that their function as courts of equity is brought into play. *Matter of Casualty Co. (Ruvin Claim)*, 244 N. Y. 443; *Matter of New York Title & Mortgage Co.*, 168 Misc., 60; *Matter of New York Title & Mortgage Co.*, 171 Misc. 489; *Matter of Lawyers Mortgage Co.*, 169 Misc. 802, *aff'd*, 256 App. Div. 974.

the New Company's stock is worth much more than the PDC's estimates would indicate.

While the case was before the District Court of Appeal, one of the country's leading financiers, Mr. Clint W. Murchison of Dallas, Texas, offered to pay $17,000,000 to the Old Company in exchange for preferred stock and approximately one-half the equity stock *of the Old Company*. That amount would have been sufficient for non-can restorations to be completed, all other liabilities of the Old Company to be paid off, the receivership to be lifted and the New Company's stock turned back to its owner, the Old Company. The matter was brought before the District Court of Appeal; but the Court held that it could not consider the offer, and that if it could, the offer would be only "cumulative" evidence of value. (App., B 35-36).

Under color of law, with the acquiescence of State officials and the California courts, and with the participation and assistance of a group of experts of the utmost respectability, the Management of the New Company has carried out one of the most astute and best planned raids on the interests of stockholders that has ever been perpetrated in American financial history. Its dimensions stagger the imagination, and produce the natural reaction that it just cannot be so. But it is so. The Management has put itself in the position where it can continue to enjoy possession of appellants' property, and the fruits thereof, for 28 years, without paying a nickel's worth of compensation, and then, at its own convenience, can buy them out for a fraction of what their property is worth.

It is submitted that the courts below decided erroneously constitutional questions of general importance, which this Court should hear and determine on appeal.

Respectfully submitted,

ALFRED MCCORMACK,
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PEYTON FORD,
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Of Counsel.

December 21, 1955.

FILED
DEC 21 1955
HAROLD B. WILEY, Clerk

IN THE

Supreme Court of the United States

OCTOBER TERM, 1955

No. 584

FRANK GENTLES, DON F. GATES, RANDOLPH CALDWELL and FRANCIS V. NIXON,

Appellants,

vs.

F. BRITTON McCONNELL, as Insurance Commissioner of the State of California, F. BRITTON McCONNELL, Insurance Commissioner of the State of California, as Liquidator of The Pacific Mutual Life Insurance Company of California, and PACIFIC MUTUAL LIFE INSURANCE COMPANY, a California corporation,

Appellees.

ON APPEAL FROM THE SUPREME COURT OF THE STATE OF CALIFORNIA

APPENDICES TO JURISDICTIONAL STATEMENT

ALFRED McCORMACK,
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Attorneys for Appellants

PEYTON FORD,
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INDEX

PAGE

Appendix A—Opinion of the Supreme Court of California A-1

Dissenting Opinion of Justice Traynor A-16

Dissenting Opinion of Justice Carter A-21

Appendix B—Opinion of the District Court of Appeal, First District, Division Two B-1

Appendix C—Opinion of the Superior Court for Los Angeles County C-1

Appendix D—Opinion and Decision of the California Insurance Commissioner D-1

Appendix E—Pertinent Provisions of the California Insurance Code and Code of Civil Procedure E-1

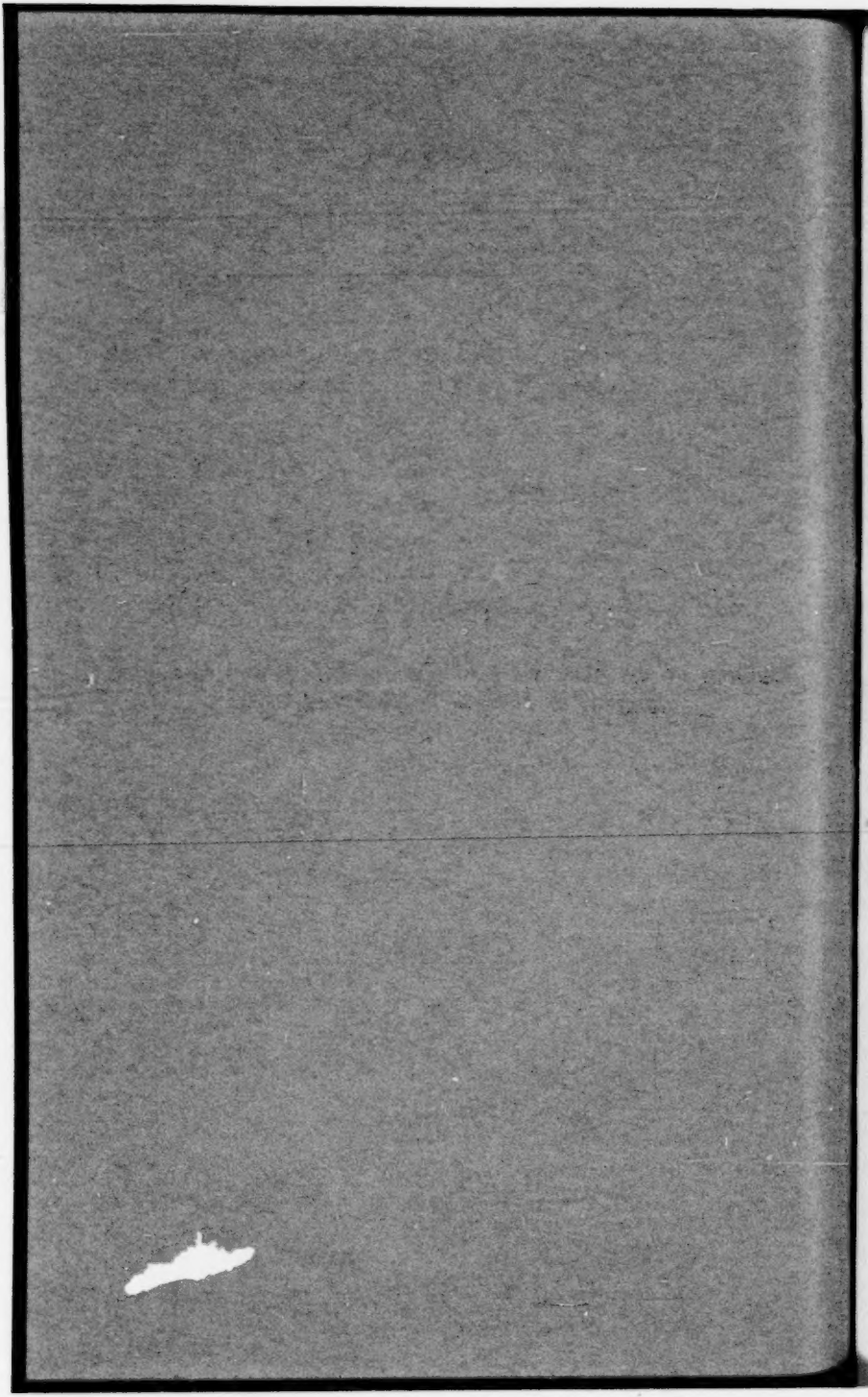
Appendix F—Rehabilitation and Reinsurance Agreement F-1

Appendix G—Report of Price Determination Committee and pertinent portions of Plan of Mutualization G-1

Appendix H—Judgment appealed from H-1

APPENDIX A

Opinion of the Supreme Court of California and dissenting opinions of Justices Traynor and Carter



APPENDIX A

Opinion of the Supreme Court of California and dissenting opinions of Justices Traynor and Carter

[L. A. No. 23261. In Bank. June 27, 1955]

The Pacific Mutual Life Insurance Company of California (a corporation) et al., appellants, v. F. Britton McConnell, etc., et al., respondents.

APPEAL from a judgment of the Superior Court of Los Angeles County. Paul Nourse, Judge. Affirmed.

Proceeding in mandamus to review action of Insurance Commissioner in approving plan for mutualization of an insurance company. Judgment denying writ affirmed.

Joseph L. Lewinson, Frank B. Belcher, C. Ray Robinson, Henry W. Low and William B. Boone for Appellants.

C. Ray Robinson and William B. Boone, as Amici Curiae on behalf of Appellants.

O'Melveny & Myers, Paul Fussell, Homer I. Mitchell, James E. Cross, George B. Gose, Frank P. Doherty, Guy Knupp and Peery Price for Respondents.

Lloyd W. Dinkelspiel and Heller, Ehrman, White & McAuliffe, as Amici Curiae on behalf of Respondents.

GIBSON, C. J.—The Pacific Mutual Life Insurance Company of California (hereinafter referred to as the "old company") and certain of its stockholders brought this mandamus proceeding in the superior court to review the action of the Insurance Commissioner in approving a plan for mutualization of a second corporation, Pacific Mutual Life Insurance Company (hereinafter called the "new company"), which had been organized by the commissioner as part of the rehabilitation of the old company. The court upheld the action of the commissioner, and plaintiffs have appealed from the judgment.

In 1936 the old company was in a hazardous and insolvent condition within the meaning of the Insurance Code, and its business and assets were taken over by the Insurance Commissioner,* as authorized by statute. (Ins. Code, §§ 1011, 1013.) Pursuant to section 1043 of the code, a rehabilitation agreement was entered into between the new company and Commissioner Carpenter, as conservator of the old company, whereby most of its assets were transferred to the new company in exchange for all the new company's capital stock. The stock was to be held by the commissioner as conservator for the benefit of the creditors, policyholders and stockholders of the old company. The new company assumed substantially all the obligations of the old company, including a limited obligation with respect to noncancellable accident and health policies (referred to herein as "non-can" policies"), and agreed to set up a special fund for restoration of benefits to holders of those policies.

In December, 1936, after a hearing, the superior court approved the rehabilitation agreement and authorized the commissioner to perform all the obligations required on his part. This order was affirmed in *Carpenter* v. *Pacific Mut. L. Ins. Co.,* 10 Cal. 2d 307 [74 P. 2d 761]. (Affd. in *Neblett* v. *Carpenter,* 305 U. S. 297 [59 S. Ct 170, 83 LEd 182].) In February, 1937, an order was made providing for the liquidation of the old company and appointing the commissioner as liquidator. It was upheld in *Carpenter* v. *Pacific Mut. L. Ins. Co.,* 13 Cal. 2d 306 [89 P. 2d 637]. In 1938 the commissioner transferred the stock of the new company to five trustees who were given legal title to the stock with power to vote it in accordance with the purposes of the rehabilitation agreement. The order approving the transfer was affirmed in *Caminetti* v. *Pacific Mut. L. Ins. Co.,* 22 Cal. 2d 344 [139 P. 2d 908].

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*Six successive commissioners, Messrs. Carpenter, Goodcell, Caminetti, Garrison, Downey and Maloney, have passed upon matters relating to the insolvency of the old company.

The rehabilitation agreement set forth the method by which a plan for mutualization of the new company could be formulated. It provided that 10 per cent of the participating life policyholders could request the new company to create an appointing committee consisting of the president of the Life Insurance Association of America, the president of Stanford University and the provost of the University of California at Los Angeles. The appointing committee was directed to select a price determination committee composed of persons skilled in matters of insurance company valuation. If the price determination committee concluded that voluntary mutualization could be practicably accomplished, it was to propose a plan of mutualization in accordance with the laws of this state. By the terms of the agreement the commissioner, as sole shareholder of the new company, consented in advance to the plan of mutualization to be formulated.

A price determination committee was appointed, consisting of Alva J. McAndless, president of the Lincoln National Life Insurance Company of Fort Wayne, Indiana; Horace R. Bassford, vice president and chief actuary of the Metropolitan Life Insurance Company of New York; Ray D. Murphy, vice president and chief actuary of the Equitable Life Assurance Society of New York; and Albert J. Hettinger, a partner in Lazard Freres and Company, a firm engaged in investment banking. After three years of study the committee proposed a plan of mutualization, which provides that, upon the occurrence of certain conditions, the new company shall buy all of its own capital stock for $3,000,000, plus interest from December 31, 1948, the price to be augmented should the restoration of benefits under the non-can policies be completed before 1973.

The proposed plan of mutualization was adopted by the directors of the new company on May 5, 1950. On September 22, 1950, after a hearing, Commissioner Downey ap-

proved the plan, finding that it would be fair and equitable in its operation, and thereafter it was approved by the policyholders of the new company. This proceeding in mandamus was then brought to review the action of the commissioner, and the trial court concluded that there was substantial evidence to support his findings and that he had not exceeded his jurisdiction or abused his discretion in approving the plan.

Plaintiffs attack the judgment upon numerous grounds, and, although many of their contentions may be disposed of by application of principles of res judicata, we believe that the problems may be more clearly presented by first discussing the propriety of the determination of the various points without regard to the binding effect of prior adjudications.

The first problem which we must consider is whether the proper statutes were followed in the formulation and approval of the mutualization plan. As contemplated by the rehabilitation agreement, all steps in connection with the adoption of the plan were taken pursuant to section 11525 et seq. of the Insurance Code, which relate to voluntary mutualization of a solvent insurer.* Plaintiffs assert that the applicable statutes for mutualization of the new company are sections 1043 et seq., which govern involuntary mutualization of an insolvent insurer.† The essential dif-

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*Section 11525 of the Insurance Code provides: "A solvent domestic incorporated insurer having a paid-in capital represented by outstanding shares of capital stock and issuing, on a reserve basis, nonassessable policies of life insurance or of both life and disability insurance, may convert itself into an incorporated mutual life insurer, or life and disability insurer, issuing nonassessable policies on a reserve basis. To that end it may provide and carry out a plan for the acquisition of the outstanding shares of its capital stock for the benefit of its policyholders, or any class or classes of its policyholders, by complying with the requirements of this chapter."

Sections 11526-11533 contain detailed provisions relating to procedure for adoption and execution of the plan of mutualization.

†Section 1043 of the Insurance Code provides in part: "In any proceeding under this article, the commissioner, as conservator or as

ferences in procedure are that under the sections relating to voluntary mutualization of a solvent company the plan is adopted by the directors, subject to approval by the stockholders and the commissioner, and no court proceedings are necessary; whereas under the provisions for involuntary mutualization of a seized insurer the plan is formulated by the commissioner as conservator without consent of the stockholders or directors, and it must be approved by the court.

The new company is solvent and nondelinquent, and there is no sound reason why it should be mutualized under the statutes relating to insolvent insurers. The commissioner had power to create the new corporation in order to preserve the business of the seized insurer. Section 1043, which authorizes the commissioner to enter into rehabilitation agreements, contains no express limitation on what may be included in them, and section 1037 provides that the enumeration of the powers of the commissioner shall not be construed as a limitation upon him or upon his right to do such other acts as he may deem necessary in connection with the handling of the affairs of an insolvent company.*

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liquidator, may, subject to the approval of said court, and subject to such liens as may be necessary mutualize or reinsure the business of such person, or enter into rehabilitation agreements." The words "such person" include an insolvent insurer as referred to in sections 1010 et seq. of the Insurance Code dealing with insolvency and delinquency.

Section 1045 provides: "If at any time after the issuance of an order under section 1011 . . . it shall appear to the commissioner that the purposes of section 1011 can be best attained by the mutualization of such life insurer, the commissioner may formulate a plan for the mutualization of such insurer." Section 1046 et seq. set forth the necessary procedural steps.

*Section 1037 of the Insurance Code provides in part: "The enumeration, in this article, of the duties, powers and authority of the commissioner in proceedings under this article shall not be construed as a limitation upon the commissioner, nor shall it exclude in any manner his right to perform and to do such other acts not herein specifically enumerated, or otherwise provided for, which he may deem necessary or expedient for the accomplishment or in aid of the purpose of such proceedings."

When salvaging the business of a seized insurer the greatest possible protection should be given to creditors and other interested parties, and in the present instance the commissioner evidently concluded that this objective could best be accomplished through the formation of a new company divorced as far as possible from the control of those who were in charge of the old company when it experienced financial difficulties.

The new company is a separate and distinct entity, and when the business was transferred it ceased to be the business of the old company and became the business of the new company. In *Garrison* v. *Pacific Mut. L. Ins. Co.*, 83 Cal. App. 2d 1, 9-10 [187 P. 2d 893], it was held that the identity of the new company "is utterly distinct from that of old company," that it "cannot be fairly said that it is a continuance of old company," and that the new company "is a separate entity that came into being after old company's insolvency was declared. . . ." The fact that the new company may for some purposes have served as an agent or instrumentality of the commissioner does not destroy its identity as a separate company. Accordingly, as contemplated by the rehabilitation agreement, the applicable statutory provisions for mutualization of the new company are those found in section 11525 et seq., which govern voluntary mutualization of solvent nondelinquent insurers.

Plaintiffs nevertheless contend that it was improper to follow the procedure set up in the code for mutualization of a solvent company because, they assert, the commissioner in doing so was forced to act in a dual capacity with conflicting interests. Section 11526, which prescribes the method to be followed in mutualizing a solvent insurer, provides that the plan shall be: ". . . . (b) Approved by the vote of the holders of at least a majority of the outstanding shares at a special meeting of shareholders called for that purpose, or by the written consent of such shareholders.

(c) Submitted to the commissioner and approved by him in writing." Commissioner Carpenter as the sole holder of the stock of the new company consented in advance to the plan of mutualization, and Commissioner Downey approved it after holding a hearing to ascertain if the plan would be fair and equitable in its operation. Plaintiffs claim that the responsibilities of the commissioner under subdivision (c) are different from and may conflict with his duties under subdivision (b). Even if there might be such a conflict under some circumstances, it would not follow that it was improper to adopt the statutory procedure set forth for the mutualization of a solvent company. The legislative scheme for the mutualization of solvent nondelinquent insurers would in some instances be defeated if the commissioner were disqualified for the reasons urged by plaintiffs, and it must be assumed that the Legislature realized that the commissioner might be required to pass upon the fairness of a plan in a case where he, acting as conservator, had previously consented to mutualization on behalf of the stockholders. In numerous cases where the action of an administrative officer was necessary to prevent defeat of the statutory scheme, his participation has been upheld, although the grounds for disqualification were much more serious than those raised here. (For example, see *Thompson* v. *City of Long Beach,* 41 Cal. 2d 235, 243-244 [259 P. 2d 649]; *Caminetti* v. *Pacific Mut. L. Ins. Co.,* 22 Cal. 2d 344, 365-366 [139 P. 2d 908]; *Federal Const. Co.* v. *Curd,* 179 Cal. 489, 493-495 [177 P. 469, 2 A. L. R. 1202]; *Scannell* v. *Wolff,* 86 Cal. App. 2d 489, 492-493 [195 P. 2d 536]; *Nider* v. *Homan,* 32 Cal. App. 2d 11, 13 [89 P. 2d 136].) The fact that Commissioner Carpenter gave advance consent on behalf of the stockholders to a plan of mutualization did not disqualify Commissioner Downey from passing upon the fairness of the mutualization plan which was promulgated.

An alternative reason for rejecting plaintiffs' claim that it was improper to follow the procedure set forth in section 11525 et seq. in the mutualization of the new company is that the validity of the rehabiliation agreement, which provided for voluntary mutualization, is now res judicata. A copy of the agreement was attached to and made a part of the petition which sought approval of the agreement. The petition was filed pursuant to section 1043, which provides that rehabilitation agreements entered into by the commissioner are subject to the approval of the superior court. The validity of all the provisions of the agreement was put in issue by the petition and determined by the court. The order of December 4, 1936, approved the agreement "and each and all of the terms and conditions thereof, and the plan therein embodied," reciting that all interested parties had been given a reasonable opportunity to be heard on "the question of fairness, justice, equity, feasibility, and propriety" of the agreement and the plan. All parties were forever enjoined from making any complaint with respect to the agreement or any provisions thereof. This order was affirmed in *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal. 2d 307 [74 P. 2d 761]. (See also *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 13 Cal. 2d 306, 314-316 [89 P. 2d 637]; *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal. 2d 344, 351-352 [139 P. 2d 908].)

While different causes of action were involved in the present proceeding and the one leading to the order approving the rehabilitation agreement, the parties were the same, and it is settled that even though the causes of action be different, the prior determination of an issue is conclusive in a subsequent suit between the same parties as to that issue and every matter which might have been urged to sustain or defeat its determination. (*Shore* v. *Shore*, 43 Cal. 2d 677, 682 [277 P. 2d 400]; *Krier* v. *Krier*, 28 Cal. 2d 841, 843 [172 P. 2d 681]; *De Hart* v. *Allen*, 26 Cal. 2d 829, 831

[161 P. 2d 453]; *Estate of Keet,* 15 Cal. 2d 328, 334 [100 P. 2d 1045]; *Sutphin* v. *Speik,* 15 Cal. 2d 195, 201 et seq. [99 P. 2d 652, 101 P. 2d 497]; *Caminetti* v. *Board of Trustees,* 1 Cal. 2d 354, 356 [34 P. 2d 1021]; *Price* v. *Sixth District Agri. Assn.,* 201 Cal. 502, 510 et seq. [258 P. 387].) Inconsistent language found in certain opinions of the District Court of Appeal must be disapproved. (*Green* v. *Green,* 66 Cal. App. 2d 50, 59 [151 P. 2d 679]; *Babcock* v. *Babcock,* 63 Cal. App. 2d 94, 97 [146 P. 2d 279]; *Bank of America* v. *McLaughlin,* 22 Cal. App. 2d 411, 417 [71 P. 2d 291, 72 P. 2d 554].) The basic issue before the court when the agreement was submitted for approval was the propriety of each of its provisions, and the determination of that issue is conclusive as to every matter which might have been urged to sustain or defeat its determination.

It is contended that the order approving the rehabilitation agreement may be collaterally attacked upon the theory that the mutualization procedure provided for in the agreement followed the wrong statutory provisions and that therefore the order is void. For the purpose of passing upon this question we shall assume, contrary to what we have just decided, that the wrong statutes were used in the mutualization of the new company.

It is the general rule that a final judgment or order is res judicata even though contrary to statute where the court has jurisdiction in the fundamental sense, i. e., of the subject matter and the parties. In the consideration of problems arising in this field it should be kept in mind that there is a difference between lack of jurisdiction in the fundamental sense, which is ordinarily essential for collateral attack, and the broader meaning of the term "lack of jurisdiction" when used in determining the availability of prohibition or certiorari to review an order or judgment. Some cases involving collateral attack have unfortunately failed to recognize this distinction. (For discussion of the

distinction, see *Abelleira* v. *District Court of Appeal,* 17 Cal. 2d 280, 287-291 [109 P. 2d 942, 132 A. L. R. 715]; *Tide Water Assoc. Oil Co.* v. *Superior Court,* 43 Cal. 2d 815, 821 [279 P. 2d 35].)

In some instances the requirements of a statute may relate to subject matter jurisdiction, and disregard of the statute may render a judgment void and subject to collateral attack. (See, for example, *Grannis* v. *Superior Court,* 146 Cal. 245, 254-255 [79 P. 891, 106 Am. St. Rep. 23]; *cf. Rogers* v. *Cady,* 104 Cal. 288, 291-292 [38 P. 81, 43 Am. St. Rep. 100] [constitutional provision].) In the present case, however, it is clear that the court which approved the rehabilitation agreement had jurisdiction of the subject matter and the parties, and, unless the case comes within some exception, collateral attack cannot be based on the ground that the court authorized mutualization to proceed under the wrong statute.

Closely analogous to the problem involved here are cases holding that probate decrees are res judicata, although they direct distribution pursuant to wills which are contrary to statute, since the court sitting in probate, like a court passing upon a rehabilitation agreement, is under a duty to determine the validity of the instrument before it. (*Estate of Loring,* 29 Cal. 2d 423, 427 et seq. [175 P. 2d 524]; *Crew* v. *Pratt,* 119 Cal. 139, 147 et seq. [51 P. 38]; *Estate of Gardiner,* 45 Cal. App. 2d 559, 562 et seq. [114 P. 2d 643]; *McGavin* v. *San Francisco P. O. A. Soc.,* 34 Cal. App. 168, 170 et seq. [167 P. 182]. Similarly analogous are cases holding that an order settling a trustee's account is res judicata as to the propriety of the purchase of investment certificates which were issued contrary to statute. (*Willson* v. *Security-First Nat. Bank,* 21 Cal. 2d 705 [134 P. 2d 800]; *Estate of Crane,* 73 Cal. App. 2d 93 [165 P. 2d 940]; *cf. Fergodo* v. *Donohue,* 40 Cal. App. 670 [181 P. 819].) *Estate of Rowe,* 66 Cal. App. 2d 594 [152

P. 2d 765], which is contrary to the cases cited above, is disapproved.

The principle of res judicata has also been applied as a basis for holding that judgments enforcing contracts are a bar to the defense of illegality in subsequent litigation. (*Andrews* v. *Reidy*, 7 Cal. 2d 366 [60 P. 2d 832]; *De Hart* v. *Allen*, 49 Cal. App. 2d 639, 646 [122 P. 2d 273], approved in *De Hart* v. *Allen*, 26 Cal. 2d 829, 830-831 [161 P. 2d 453]; *cf. Short* v. *Short*, 106 Cal. App. 210, 215 [288 P. 1111].) Another instance in which the doctrine was applied is *San Diego Trust & Sav. Bank* v. *Young*, 19 Cal. 2d 98 [119 P. 2d 133], where the prior judgment reduced the time for redemption contrary to statute. The San Diego case impliedly overruled *Anthony* v. *Janssen*, 183 Cal. 329 [191 P. 538], and *Tonningsen* v. *Odd Fellows' Cemetery Assn.*, 60 Cal. App. 568 [213 P. 710]. It has also been held that a judgment, which was contrary to the Constitution because it was based upon a statute later held invalid, was nevertheless res judicata in a subsequent suit, the court stating that objections to the statute should have been raised in the prior proceeding. (*Chicot County Drainage Dist.* v. *Baxter State Bank*, 308 U. S. 371, 376, 378 [60 S. Ct. 317, 319-320, 84 L. Ed. 329].) The Chicot case is quoted with approval in *Mueller* v. *Elba Oil Co.*, 21 Cal. 2d 188, 205-206 [130 P. 2d 961], and was cited in *Rescue Army* v. *Municipal Court*, 28 Cal. 2d 460, 463-464 [171 P. 2d 8].

There are some recognized exceptions to the general rule that collateral attack will not be allowed where there is fundamental jurisdiction even though the judgment is contrary to statute. For example, a judgment may be collaterally attacked where unusual circumstances were present which prevented an earlier and more appropriate attack. (See 1 Witkin, California Procedure (1954), 411-412.) In *Burtnett* v. *King*, 33 Cal. 2d 805 [205 P. 2d 657, 12

A. L. R. 2d 333], collateral attack was permitted against a default divorce decree which awarded all the community property to the plaintiff in the absence of a prayer therefor in the complaint contrary to the provision in section 580 of the Code of Civil Procedure that relief in a default case cannot exceed that demanded in the complaint. The defendant in the divorce action had no notice or warning that the property would be affected by a default judgment, and the opinion points out that the decision would sanction a trap if it held that his property rights had been disposed of since he would properly have assumed from the complaint that his rights to the property were not to be litigated at that time. (33 Cal. 2d at p. 811.) The present case is readily distinguishable, since there was nothing to prevent the questions which are raised with regard to the validity of the rehabilitation agreement from being litigated in the proceedings which led to the order approving the agreement.

Proceedings to prohibit or annul judgments of contempt for violation of injunctions and other equitable orders made contrary to statute may constitute another exception to the general rule. (*Harlan* v. *Superior Court*, 94 Cal. App. 2d 902, 904-905 [211 P. 2d 942]; *Hunter* v. *Superior Court*, 36 Cal. App. 2d 100 [97 P. 2d 492]; *cf. Fortenbury* v. *Superior Court*, 16 Cal. 2d 405, 407-408 [106 P. 2d 411] [violation of Constitution].) The decisions do not use the term, but the attack in such cases might be considered to be collateral, and the proceedings apparently fall in a special category because they are penal in nature.

From the foregoing discussion it follows that, even if we assume that the rehabilitation agreement and the order approving it authorized mutualization of the new company under the wrong statutes, the order is nevertheless res judicata.

The next problem is whether there was sufficient compliance with the statutory requirements for voluntary mutualization of solvent insurers. Section 11525 et seq.

provide that the plan of mutualization shall be adopted by the directors and approved by the shareholders, the commissioner and the policyholders. Plaintiffs contend that the actions taken to meet these requirements were in certain respects defective and unauthorized.

The approval of the shareholders to the plan of mutualization was given in the rehabilitation agreement by Commissioner Carpenter as sole stockholder of the new company. As we have seen, the agreement provided for the formulation of a plan of mutualization by the price determination committee, and plaintiffs claim that the commissioner, acting for the shareholders of the new company, was without authority to give advance consent to such a plan. In the absence of statutory provision to the contrary, the stockholders of a solvent company can contract to consent to a future plan of voluntary mutualization (*cf. Market St. Ry. Co.* v. *Hellman,* 109 Cal. 571, 586-587 [42 P. 225]), and no sound reason appears why such an agreement is improper merely because the shares are held by the commissioner as conservator of a seized insurer. The commissioner apparently concluded that a plan for mutualization which could not be destroyed by future action or nonaction of the shareholders was necessary as a means of inducing both former and prospective policyholders to deal with the new company and thus permit its continued existence. The powers vested in the commissioner by sections 1037 and 1043 are sufficiently broad to authorize him, as sole stockholder, to give advance consent to the plan of mutualization. Moreover, the validity of all portions of the rehabilitation agreement, including the provision for advance consent, is res judicata.

The directors adopted the mutualization plan, but it is claimed that the action taken was ineffective because they assertedly did not obtain sufficient information to enable them to properly evaluate the desirability of the plan. They

had the benefit of the report of the price determination committee and the opinions of experts, including actuaries and officers of the company, and it seems obvious that, as a practical matter, directors must ordinarily act on the advice of corporate officers and other persons who have expert knowledge. (See Ballantine & Sterling, California Corporation Laws (1949), p. 110.)

After the directors adopted the plan as formulated by the price determination committee, Commissioner Downey held a hearing which lasted nearly three weeks. Oral and documentary evidence was received, and all interested parties had an opportunity to participate. The commissioner approved the plan after finding that the rights and interests of the new company, its policyholders and shareholders were protected and that the plan would be fair and equitable in its operation. Plaintiffs contend that the findings are not supported by the evidence and that there was a lack of procedural due process at the hearing. In passing upon these contentions, we shall first give consideration to plaintiffs' claim that the trial court, in reviewing the action of the commissioner, should have held a trial de novo. The approval of the mutualization plan by the commissioner did not involve any deprivation of property rights or vested rights; it was in essence a permit or license authorizing the new company to purchase its own stock. Under these circumstances the function of the superior court was to determine whether the action taken by the commissioner was arbitrary or constituted an abuse of discretion, and in upholding the action of the commissioner, it properly refused to conduct a trial de novo. (*Southern Calif. Jockey Club, Inc.* v. *California etc. Racing Board*, 36 Cal. 2d 167, 174-175 [223 P. 2d 1]; *McDonough* v. *Goodcell*, 13 Cal. 2d 741, 746-749 [91 P. 2d 1035, 123 A. L. R. 1205]; see *Thomas* v. *California Emp. Stab. Com.*, 39 Cal. 2d 501, 504 [247

P. 2d 561]; *Andrews* v. *State Board of Registration,* 123 Cal. App. 2d 685, 694-695 [267 P. 2d 352].)

There is no merit in plaintiffs' claim that the record before the commissioner does not support his approval of the plan. The price determination committee consisted of men highly skilled in matters of insurance company valuation, and they were assisted in the formulation of the plan by Joseph Christman, associate actuary of the Metropolitan Life Insurance Company of New York, two Fellows of the Society of Actuaries, and numerous trained supervisory and clerical employees. Experts testified that the price fixed for the purchase of the stock was fair, that the provisions relating to the time and manner of payment were necessary for the safety and stability of the new company, that the proposed plan gave due regard and protection to the rights of all persons interested in the new company and would be fair in its operation.

Plaintiffs' contention that there was a denial of procedural due process is based on their claim that the commissioner accepted the conclusions of the price determination committee without having before him all the facts on which those conclusions were based and that the committee itself relied on statistics furnished by its actuary without reviewing all the supporting data. Two members of the price determination committee testified in detail as to how the committee arrived at its determinations, and the actuary testified regarding his report which was introduced in evidence. Thus two of the four members of the committee who were responsible for its report, as well as the actuary who procured most of the data relied on by the committee, were available for cross-examination. These men, as we have seen, were experts in the insurance and investment fields, and the fact that the other members of the committee and the persons who assisted the actuary were not called as witnesses is immaterial, at least in the ab-

sence of a showing that plaintiffs sought to obtain their testimony. (*City of Pasadena* v. *City of Alhambra,* 33 Cal. 2d 908, 919 [207 P. 2d 17]. At the hearing an offer was made to furnish the documents and testimony necessary to explain every detail of the committee's work. No claim is made that any request for data was refused, and plaintiffs have no valid basis for complaint if they failed to make such a request.

The judgment is affirmed.

Shenk, J., Spence, J., and Wood (Fred B.), J. pro tem.,* concurred.

TRAYNOR, J.—I dissent.

Although the Legislature has provided detailed statutory provisions for the mutualization of the business of an insolvent insurer (Ins. Code, § 1045 et seq.), the majority opinion holds in effect that these provisions may be completely nullified by the execution of a rehabilitation agreement under section 1043 of the Insurance Code, if such agreement provides for the voluntary mutualization of a new insurer created for the purpose of carrying on the business of the old. The commissioner has broad powers in executing rehabilitation agreements, and it may be both proper and desirable for him to make use of a new corporate entity to salvage the business of an insolvent insurer. It does not follow, however, that if the end product of a rehabilitation agreement is to be the mutualization of the business of an insolvent insurer, the statutory provisions with respect to such mutualization may be ignored. To hold that they may be not only renders the provisions with respect to involuntary mutualization superfluous but deprives the interested parties of their right to the protection

*Assigned by Chairman of Judicial Council.

of court scrutiny of the plan of mutualization. (See Ins. Code, § 1051.)

The importance to the shareholders of the old company of having the court independently pass upon the fairness of the plan of mutualization is demonstrated by the facts of this case. The trial court clearly indicated that had the decision been his, the plan would not have been approved; if the shareholders were entitled to his independent judgment, their rights have been prejudiced by his failure to exercise it. This case is not one involving only the mutualization of a solvent insurer, since if it were, the shareholders would have the power to protect their interests by withholding their consent to the plan of mutualization. (Ins. Code, § 11526, subd. (b).) In fact, the business of an insolvent insurer is being mutualized pursuant to a rehabilitation agreement that has deprived the shareholders of the old company of the veto power they otherwise would have, and under the holding of the majority opinion they must look to the commissioner rather than to the court for the protection of their interests. (Ins. Code, §§ 11526, subd. (c), 11527.) Although the Legislature recognized that approval by the commissioner is sufficient when all of the interested parties are in a position to protect their own interests, it also provided that court approval is essential when they are not. (Ins. Code, § 1051.)

Despite the force of the foregoing considerations, if in fact the trial court in 1936 approved a rehabilitation agreement that not only provided for mutualization contrary to the statutory provisions but also restricted the power of that court to control the ultimate disposition of the assets in the hands of the commissioner as conservator or liquidator, I would reluctantly concur in the judgment on the ground that the validity of the agreement and order is res judicata. In my opinion, however, the court in 1936 did not exhaust its power to control the disposition of

assets in the hands of the commissioner as conservator or liquidator (see Ins. Code, § 1037, subd. (d)) and that therefore the commissioner cannot carry out the terms of the mutualization agreement until as liquidator he has secured the permission of the court in the insolvency proceedings. Accordingly, until he secures that approval he cannot approve the plan presented by the price determination committee as "fair and equitable in its operation" (Ins. Code, § 11527), for it cannot be known whether it will become operative at all until it is approved by the court in the insolvency proceedings.

Subdivision (d) of section 1037 provides "that no transaction involving real or personal property shall be made where the market value of the property involved exceeds the sum of one thousand dollars without first obtaining permission of . . . [the court in the insolvency proceedings], and then only in accordance with such terms as said court may prescribe." The stock of the new company subject to the plan of mutualization is personal property worth more than $1,000, and that plan is clearly a transaction involving such property. This section has not been complied with unless the court in approving the rehabilitation agreement granted permission to the commissioner to dispose of the stock under the terms of any mutualization agreement that might be proposed by the price determination committee 10 years or more in the future.

The order approving the rehabilitation agreement is ambiguous. Paragraph 15 provides:

"That the Insurance Commissioner of the State of California as Conservator of respondent corporation, or, if he should hereafter be appointed Liquidator of said corporation, as such Liquidator, be and is hereby authorized, without further order of this court, fully and faithfully to perform, carry out, and discharge each and all of the obligations, terms, conditions, and covenants on his part required

to be performed under the terms of said Rehabilitation and Reinsurance Agreement; and, either with or without further order of this court, to make, do, execute, and deliver any and all such further or other acts, deeds, and things by him deemed reasonably necessary or desirable to effectuate the intents and purposes of said Rehabilitation and Reinsurance Agreement, and to assure and to confirm to Pacific Mutual Life Insurance Company, or its successors, all and singular the properties hereinbefore directed to be conveyed and released to said corporation, and to enable said corporation from and after the date hereof to conduct and continue to conduct a life and disability insurance business, as contemplated by said agreement."

Paragraph 16 provides:

"That this court, without relinquishing by these specific provisions any jurisdiction by it retained as a matter of law, do, and it does hereby, specifically retain and reserve jurisdiction of the within proceedings (for the purpose of authorizing or approving any act of the Insurance Commissioner of the State of California done, or to be done pursuant to or in accordance with this order, and) for the purpose of making or entering, upon application of the Insurance Commissioner of the State of California or of Pacific Mutual Life Insurance Company, any order, decree, judgment, or ruling required, permitted, or requested to be done, made, or entered in connection with or pursuant to the terms of said agreement, or for the effectuation of the purposes thereof."

Since the contemplated plan of mutualization was not to be formulated for at least 10 years, the court could obviously not approve that plan at the time it entered its order approving the rehabilitation agreement. Moreover, it did not expressly approve in advance the carrying out of any mutualization plan that might be presented by the price determination committee. Although standing alone

the language permitting the commissioner to carry out the rehabilitation agreement "without further order of this court" might be interpreted as exhausting the court's jurisdiction over mutualization, it may not reasonably be so interpreted in the light of the express reservation of jurisdiction "for the purpose of making . . . any order . . . required . . . in connection with or pursuant to the terms of said agreement." It is significant that in *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal. 2d 307, 322 [74 P. 2d 761], this court was careful to note: "The plan also provides that the commissioner, either as conservator or liquidator, shall continue to hold all the stock of the new company as a protection to all old company policyholders. Ultimate mutualization, in the event the policyholders so elect is also provided for. The trial court reserves jurisdiction over the entire proceeding." Paragraphs 15 and 16 may be reconciled by interpreting them as authorizing the commissioner without further order of the court to carry out the rehabilitation agreement to the extent that its provisions represented a completed plan for rehabilitation and reinsurance, and at the same time reserving to the court jurisdiction to approve or disapprove plans to be developed in the future for mutualization or other disposal of the stock in the hands of the commissioner. Such an interpretation of the order subserves the primary purpose of section 1037, subdivision (d), and the statutes governing involuntary mutualization by securing to all interested parties their right to court scrutiny of all steps in the proceedings that substantially affect their rights, and since the order is reasonably susceptible of that interpretation it should be adopted. Although the validity of the rehabilitation agreement and the order approving it are res judicata, the interpretation of the order is not res judicata, and it should not be interpreted to sanction further departures from the statutory provisions than res judicata compels. (See *Wat-*

son v. *Lawson,* 166 Cal. 235, 242 [135 P. 961]; *Treece* v. *Treece,* 125 Cal. App. 726, 728 [14 P. 2d 95].)

The judgment should be reversed.

Schauer, J., concurred.

CARTER, J.—I dissent.

The majority opinion is a masterpiece of legal legerdemain. It approves a transaction whereby the policyholders of old company are deprived of between $18,000,000 and $24,000,000 to which they are entitled under any concept of law and justice. It also deprives the stockholders of old company of whatever value their stock in old company may be worth in view of the fact that the assets of old company which were transferred to new company at the time of its creation were valued in excess of over $200,000,000. The majority concedes that new company was created in an insolvency proceeding and has always been used in said proceeding as an agency of the insurance commissioner for the purpose of rehabilitating an insolvent insurance company, and that such proceeding is still pending because rehabilitation has not been completed. It nevertheless holds that "the new company is solvent and nondelinquent," even though it owes and is obligated to pay the policyholders of old company between $18,000,000 and $24,000,000 which it admittedly is not financially able to pay. In approving this transaction the majority disregards express statutory provisions of this state and deprives the stockholders and policyholders of old company of their right to a judicial review of the administrative proceeding whereby they were deprived of their property, thus denying them due process of law to which they are entitled under both state and federal constitutional provisions.

The Undeniable Facts

On July 22, 1936, some 3,000 stockholders and 300,000 policyholders of The Pacific Mutual Life Insurance Company of California, hereinafter known as old company, were stunned by the news that the insurance commissioner had taken charge of the company, alleging it to be insolvent. This development was all the more shocking because of its suddenness and also because only a short time before, the regular, verified, annual statement of the company showed it to be in sound financial condition, as had similar previous statements from year to year consistently shown throughout its lifetime of over 68 years. The business and assets of old company were then taken over by the insurance commissioner of this state pursuant to the provisions of sections 1011 and 1013 of the Insurance Code. Thereafter, The Pacific Mutual Life Insurance Company was organized as part of a plan of rehabilitation of old company by the commissioner who purchased its entire capital stock with assets of old company. Pursuant to section 1043 of the Insurance Code, a "Rehabilitation and Reinsurance" agreement was entered into between the new company and the then insurance commissioner, as conservator of old company. The rehabilitation plan provided for the organization of a new corporation with a capital of $1,000,000 which consisted of 10,000 shares at a par value of $100 each. The commissioner was to purchase all the outstanding stock of the new company with $3,000,000 in cash belonging to the old company (which gave new company an initial surplus of $2,000,000). The commissioner was then to transfer all the other assets of old company (with the exception of the stock of new company which, of course, was owned by old company) to new company, and new company was to assume all policies and obligations of the old company to the extent provided for in the plan. The plan provided that

new company would assume all the obligations of the old company under existing policies with the exception of the non-can policies, which obligations were assumed on a reduced benefit schedule at the old premium rates. It was agreed that further benefits would be restored out of certain designated income of new company. *All of new company's stock was purchased with $3,000,000 out of old company's funds.* In addition, all the other assets of old company (over $200,000,000 assets in addition to going agency organization and concern, good will, etc., "worth several millions of dollars" [*Carpenter* v. *Pacific Mut. L. Ins. Co.,* 10 Cal. 2d 307, 325 (74 P. 2d 761)] were transferred to new company. Therefore, new company owes its creation and existence to old company. The confiscatory nature of this entire proceeding, including the present majority holding, is at once apparent when we see that old company's stockholders will ultimately only receive $3,000,000 for their stock which, when old company was taken over, was supported by that amount in cash *plus* over $200,000,000 in various assets plus the value of good will, going business organization, etc., worth several millions of dollars! The agreement thus provided for a transfer to new company of the assets of old company (with certain exceptions not relevant here) and the assumption by new company of the obligations of old company, excluding certain noncancellable policies. With regard to these policies, known as the "non-can" policies, new company assumed a limited obligation and agreed to set up a special fund for the restoration of benefits thereunder. This obligation is still unpaid and outstanding. The capital stock of new company was to be held by the commissioner, as conservator, or liquidator, for the benefit of the creditors, policyholders, and stockholders of old company. On December 4, 1936, the agreement was approved by the trial court. In *Carpenter* v. *Pacific Mut. L. Ins. Co.,* 10 Cal. 2d 307, 332, 334 [74 P.

2d 761] (affirmed *Neblett* v. *Carpenter,* 305 U. S. 297 [59 S. Ct. 170, 83 L. Ed. 182]), it was held that the organization of new company, as part of a plan to rehabilitate the business of old company was proper. It is pointed out (p. 322) that "Ultimate mutualization, in the event the policyholders so elect is also provided for."

On February 2, 1937, an order was made providing for the liquidation of the old company and appointing the insurance commissioner as liquidator. This order was upheld on appeal (*Carpenter* v. *Pacific Mut. L. Ins. Co.,* 13 Cal. 2d 306 [89 P. 2d 637]), although old company has never been dissolved. On April 4, 1938, the commissioner, as liquidator, transferred title to the capital stock of new company to voting trustees. This transfer was upheld on appeal (*Caminetti* v. *Pacific Mut. L. Ins. Co.,* 22 Cal. 2d 344 [139 P. 2d 908]). (Other aspects of this case have been decided by this court in *Caminetti* v. *Pacific Mut. L. Ins. Co.,* 22 Cal. 2d 77 [136 P. 2d 779]; *Caminetti* v. *Pacific Mut. L. Ins. Co.,* 22 Cal. 2d 386 [139 P. 2d 930]; *Caminetti* v. *Pacific Mut. L. Ins. Co.,* 23 Cal. 2d 94 [142 P. 2d 741]; *Neblett* v. *Pacific Mut. L. Ins. Co.,* 22 Cal. 2d 393 [139 P. 2d 934]; *Carpenter* v. *Pacific Mut. L. Ins. Co.,* 14 Cal. 2d 704 [96 P. 2d 796]; and by the appellate courts in *Sanborn* v. *Pacific Mut. L. Ins. Co.,* 42 Cal. App. 2d 99 [108 P. 2d 458]; *Garrison* v. *Pacific Mut. L. Ins. Co.,* 83 Cal. App. 2d 1 [187 P. 2d 893].)

New company now seeks to acquire its stock (see later discussion) through the device of mutualization under section 20(a) of the rehabilitation agreement. The mutualization plan provides that the price to be paid for new company's stock is $3,000,000, with simple interest. If noncan benefits are fully restored prior to January 1, 1973, the purchase price is to be increased by an additional sum of $250,000 for each full year by which the date of completion of restoration precedes December, 1973. The pur-

chase price is not absolutely payable, but is to be paid only "when and if" all the following conditions are met: (1) Non-can restoration is completed; (2) the funds in a special surplus fund (to be created pursuant to the plan) plus the capital and surplus of new company, equal or exceed the purchase price of the stock; (3) the *financial condition* of the *new company* is such that, after paying for and cancelling the stock, it would still have admitted assets in excess of all its liabilities amounting to the sum of 4 per cent of all admitted assets plus 25 per cent of the premiums collected during the preceding calendar year on all group insurance written on a one-year term basis and on all accident and health insurance.

This resumé shows that the new company was brought into existence as a creature of the state to rehabilitate old company and to carry on its business for that purpose. It also shows the grievous injustice being perpetuated by the majority in approving the plan of mutualization used here —that of *voluntary* mutualization of an *insolvent* corporation. This type of voluntary mutualization is as voluntary as a confession given under force, duress, and threats of bodily injury. Non-can benefits have not been fully restored; even under the mutualization plan it is contemplated they will not be fully restored (if partial benefit payments can be considered "full" restoration) until 1973. Until such time as they are restored, new company cannot be considered as a solvent concern since it still owes a debt to the policyholders and stockholders of old company, which it admittedly *cannot now pay*. The amount of this debt is conceded to be between $18,000,000 and $24,000,000. How can it then be said, with any degree of honesty whatsoever, that new company is solvent and may avail itself of the statutory provisions relating to mutualization? I defy anyone to give an affirmative answer to this question.

PRESENT PROCEEDING

Purporting to act under paragraph 20(a) of the rehabilitation and reinsurance agreement, a plan of mutualization was formulated by the committee and, on September 22, 1950, the insurance commissioner found that the plan protected the rights and interests of new company, its policyholders and shareholders, and that he was satisfied that the plan would be fair and equitable in its operation.

Paragraph 20(a) of the rehabilitation and reinsurance agreement provides:

"Mutualization and Disposition of Stock of New Company

"(2) Neither the Conservator, nor, if one be appointed, the Liquidator, of the Old Company, shall dispose of any of the stock of the New Company except as follows:

"(a) At any time between July 1, 1946 and January 1, 1948, and thereafter so long as the Conservator or a Liquidator of the Old Company may continue to hold any or all of said stock, ten percent (10%) of the holders of participating policies of life insurance entitled to vote at a policy holders' election on a proposal for *voluntary* mutualization of the New Company, whether those re-insured hereunder or those issued by the New Company (each policy holder for this purpose being regarded as one person regardless of the number of policies owned or amount of insurance held) may request the New Company to create an Appointing Committee as hereinafter provided to exercise the duties and functions hereinafter specified in respect of a proposed *voluntary* mutualization of the New Company, in accordance with the laws of the State of California in effect at the time of said request, or, if said laws then so permit, of any one or more departments thereof. Such request shall specify the department or departments of the New Company desired to be mutualized.

"Upon the receipt of such request the New Company shall create an Appointing Committee consisting of the then President of the Association of Life Insurance Presidents, the President of Leland Stanford Jr. University, and the Provost of the University of California at Los Angeles, or persons occupying similar positions if their or any of their titles shall have been changed. In the event any one or more of such persons shall refuse or be unable to act, the remaining member or members shall fill the vacancy or vacancies thereby created by their appointment in writing of another person or persons of similar position and standing. If all of said persons refuse or are unable to act, the Court or any Judge thereof shall, on the application of the Commissioner, designate an Appointing Committee consisting of three (3) persons of similar position and standing. Said Appointing Committee, acting through not less than a majority of its members, shall designate a Price Determination Committee of not less than three and not more than five (5) persons skilled in matters of insurance company valuation, which committee, acting through not less than a majority thereof, shall determine whether in their opinion the proposed *voluntary* mutualization of the New Company, or of the department or departments thereof specified in said request can then be practicably accomplished *having due regard to the interests of all persons interested in the New Company.* * If it can be determined that such mutualization is not then practicable no further steps shall be taken in connection with a possible mutualization of the New Company under the provisions of this subparagraph until at least six months after the date of such determination. If in the opinion of a majority of the members of the committee such mutualization is then practicable, the committee shall determine the proper price to be

*The statutory scheme relating to insolvent companies is concerned with the protection of those interested in the *insolvent* company.

paid upon such mutualization and appropriate terms of payments thereof; said determination shall not be made, however, prior to January 1, 1947.

"If, at the date of the appointment of such committee the New Company shall have in force Participating Life Insurance written subsequent to the effective date of this agreement in an amount in excess of its Non-Participating Life Insurance written during the same period, one-half (½) of such excess shall, for the purpose of fixing the proper price to be paid (but for no other purpose) be deemed to be, and shall be valued as, Non-Participating Life Insurance. If at the time of such appointment, there shall have been transferred from the Participating Department in accordance with the provisions of sub-paragraph (d) of paragraph 6 hereof, less than ten percent (10%) of the then accrued earnings described therein, or if there shall have been transferred to the Participating Department any working capital pursuant to the provisions of subparagraph (c) of said paragraph 6, any unpaid balance thereof shall, for the purpose of fixing the proper price to be paid (but for no other purpose) be deemed to be a debt then due and matured. Said Committee shall in its report to the New Company include a plan of mutualization of the New Company, or of the department or departments thereof specified in said request of the policy holders. Such plan shall specify, in addition to any other relevant matters, the price to be paid, the terms of payment, and the persons by whom and the manner in which the right to vote the stock of the New Company is to be exercised pending complete payment of the purchase price. In this connection the said Committee, if it deem it advisable, may provide in the plan for the creation of a voting trust, designate the initial trustees, and make provision for the appointment of their successors. Unless the benefits under Non-Can policies have theretofore been fully restored and claims against the Liquidator fully paid,

such plan shall further provide that such mutualization shall not affect the provisions of paragraph 17 or of paragraph 14 hereof or the right of holders of Non-Can Policies to the restoration of benefits from the sources and in the manner therein provided.

"The New Company agrees that within sixty (60) days after the making of such report (unless said report shall be to the effect that mutualization is not then practicable) it will mail copies thereof to all of its policy holders entitled to vote upon such plan or plans of mutualization if submitted according to law. If within one hundred twenty (120) days after the mailing of such notice, ten per cent. (10%) of the policy holders entitled to vote upon any such plan or plans (each policy holder being for this purpose regarded as one person regardless of the number of policies owned or amount of insurance held) shall request in writing the submission thereof, the New Company will promptly submit the same in accordance with the laws of the State of California then in effect. The Conservator for himself and for any successors in the ownership of said stock claiming under him in any manner other than through a sale of said stock pursuant to the provisions of subparagraph (d) hereof agrees to consent and hereby consents as the holder and owner of the stock of the New Company to such plan of mutualization. In the event said mutualization plan is adopted, the Conservator, or a liquidator as aforesaid, shall dispose of such stock in accordance with such plan. The expenses of the foregoing proceedings including costs, fees and expenses of the Price Determination Committee, shall be borne by the New Company, and unless the proposed plan of mutualization is consummated, shall be charged to the Participating Department thereof.

"In the event the Price Determination Committee has been appointed as herein provided prior to January 1, 1948, said Committee shall have the power to extend the time within which mutualization may be effected hereunder for

such period or periods of time as it may deem necessary for the orderly completion of mutualization proceedings as herein ordered." (Emphasis added.)

MUTUALIZATION

The Insurance Code provides for mutualization of insurance companies in two different ways. Division 1, part 2, chapter 1, article 14, sections 1010-1062, entitled "Proceedings in Cases of Insolvency and Delinquency" provides in section 1043 for "Mutualization, reinsurance and rehabilitation." Division 2, part 2, chapter 13, article 1, sections 11525-11533, entitled "Voluntary Mutualization of Incorporated Life and Life and Disability Insurers Having a Capital Stock and Issuing Nonassessable Policies on a Reserve Basis" provides in sections 11525 and 11526 the "Authorization to mutualize" and the "Method of mutualization."

There is no dispute concerning the method actually used in this proceeding. The rehabilitation plan provided for "voluntary" mutualization and the matter proceeded under sections 11525 and 11526. There is complete disagreement as to which method should have been used. Appellants correctly contend that the procedure outlined for "involuntary" mutualization of an "insolvent" insurer is the only proper method.

As stated in *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal. 2d 307, 328 [74 P. 2d 761], ". . . the proceedings here under review were taken under sections 1010 to 1061 of the Insurance Code, adopted in 1935." (The other cases heretofore cited have reiterated this statement.) The original seizure of old company was accomplished under section 1011, subdivision (d). Section 1045 provides *"Mutualization of life insurer issuing nonassessable policies on a reverse basis: Formation of plan.* If at any time *after the issuance of an*

order under section 1011 affecting a life insurer issuing nonassessable policies on a reserve basis and organized with a capital stock evidenced by shares thereof *it shall appear to the commissioner that the purposes of section 1011 can be best attained by the mutualization of such life insurer, the commissioner may formulate a plan for the mutualization of such insurer.*" (Emphasis added.)

All proceedings heretofore had in this litigation have been as provided for in article 14 relating to insolvent and delinquent insurers. The rehabilitation agreement provides for mutualization under the statutory scheme set up for solvent insurers. The majority opinion states "The new company is solvent and nondelinquent, and there is no sound reason why it should be mutualized under the statutes relating to insolvent insurers. . . . Section 1043 [which relates to insolvents], which authorizes the commissioner to enter into rehabilitation agreements, contains no express limitation on what may be included in them, and section 1037 [which also relates to insolvents] provides that the enumeration of the powers of the commissioner shall not be construed as a limitation upon him or upon his right to do such other acts as he may deem necessary in connection with the handling of the affairs of an *insolvent company.*" (Emphasis added.) Thus the majority opinion admits the procedure relating to insolvents was the one used and impliedly admits that it is the correct procedure. However, in using the code sections relating to insolvents, the author then argues that these sections place no limitation upon the commissioner. Section 1037 provides that the powers and authority of the commissioner in proceedings *"under this article"* (which relates to insolvents) shall not be construed as a limitation on his right to act or to do that "which he may deem necessary or expedient for the accomplishment or in aid of the purpose of *such proceedings.*" Then, citing section 1043 (relating again to insolvents), we are told that the new company was prop-

erly organized by the commissioner who "evidently concluded" that the protection of creditors and "other interested parties" could best be accomplished through the formation of a new company "divorced as far as possible from the control of those who were in charge of the old company when it experienced financial difficulties." Then we are told that the new company is a separate and distinct entity. We are told this without any discussion of the character of new company, and with only the unreasoned and unsupported dictum in *Garrison* v. *Pacific Mut. L. Ins. Co.*, 83 Cal. App. 2d 1, 9-10 [187 P. 2d 893], as authority therefor.

Section 11525 (the procedure followed here) provides for "*Authorization to mutualize.* A *solvent* domestic incorporated insurer having a paid-in capital represented by outstanding shares of capital stock and issuing, on a reserve basis, nonassessable policies of life insurance or of both life and disability insurance, *may convert itself into an incorporated mutual life insurer*, or life and disability insurer, issuing nonassessable policies on a reserve basis. To that end *it may provide and carry out a plan for the acquisition of the outstanding shares of its capital stock for the benefit of its policyholders*, or any class or classes of its policyholders, by complying with the requirements of this chapter." (Emphasis added.)

The question is thus directly posed as to whether new company falls within the classification of a "solvent" domestic incorporated insurer which "may convert itself into an incorporated mutual life insurer" which "may provide and carry out a plan for the acquisition of the outstanding shares of its capital stock for the benefit of its policyholders."

Character of New Company

New company was organized by the insurance commissioner "with a name similar to that of the old company

as a corporate agent to assist him in carrying on the business of the old company" (*Carpenter* v. *Pacific Mut. L. Ins. Co.,* 10 Cal. 2d 307, 324, 325 [74 P. 2d 761]). It was also said there (p. 327) that "The proceeding was had under sections 1010 to 1061 of the Insurance Code which specially deal with the rehabilitation and liquidation of insurance companies. Those sections set up a comprehensive statutory scheme to accomplish those results. The proceeding is not one in which another party is prosecuting another party at all. It is simply a proceeding in which the state is invoking its power over a corporate entity permitted by the state to engage in a business vitally affected with the public interest upon condition of continuing compliance with the requirements provided by the state. It is not a controversy between private parties but a proceeding by the state in the interest of the public." See also *Caminetti* v. *Pacific Mut. L. Ins. Co.,* 22 Cal. 2d 77, 82 [136 P. 2d 779], where it was held that *"The new company was the corporate agency of the Insurance Commissioner as conservator for the purpose of continuing and preserving the business of the old company."* (Emphasis added.)

The commissioner held, either as conservator or later as liquidator, the entire capital stock of new company until 1938 when it was transferred to voting trustees (*Caminetti* v. *Pacific Mut. L. Ins. Co., 22* Cal. 2d 344, 356 [139 P. 2d 908]). It was there said that "The affairs of the new company are placed in charge of a board of directors to whom the agreement expressly confides a large measure of discretion. *Supervisory powers, however, are reserved to the commissioner,* independent of and in addition to his statutory powers over delinquent insurance companies. For example, no investment or reinvestment of the assets of the old company may be made without written approval of the commissioner. Payments to the restoration fund for non-can policies are subject to the approval of the commissioner who, in addition, may require further payments

thereto. The determination by the board of directors of the apportionment of expenses and the exchange of assets among the several departments of the new company is subject to adjustment by the commissioner. Reserves against policies of the old company subject to assumption or reinsurance under the agreement were to be established by the new company *with the approval of and in accordance with the requirements of the commissioner.* While as holder of the stock the commissioner possessed the voting rights incident thereto, the agreement contains no express provision with respect to the exercise of the voting power. . . .

"The trustees are given legal title to the stock of the new company with the power to exercise all the rights of ownership. *The commissioner, however, retains the entire beneficial interest for the benefit of creditors of the old company and others interested. The voting trust undertakes to transfer to the trustees only administrative duties relating to the stock, principally the right to vote the same.* . . ." (Emphasis added.)

New company does not possess the characteristics of a solvent company as that term is generally understood. First, it was organized as the *agent* of the *commissioner* to *rehabilitate* the *business* of the *old company.* It may be, as was said in the Garrison case, that it is a distinct entity without detracting in the least from the fact that it is still an agent for the purpose of rehabilitating the old company. An agent, or servant, is usually a distinct entity, but the duties and activities of such agent or servant, are carried out to serve the purposes of the principal. In other words, the agent acts for the principal, not for himself, or itself. Does the insurance commissioner ordinarily, and customarily, hold all the stock of a solvent insurance company? Does the insurance commissioner ordinarily, and customarily, have reserved to himself supervisory powers, "independent of and in addition to his statutory powers" where a solvent company is concerned? Does an insurance

commissioner ordinarily, and customarily, give his written approval of the investment or reinvestment of funds of a solvent insurance company? Does the insurance commissioner ordinarily, and customarily, tell the board of directors of a solvent company when and how they must apportion expenses and exchange assets among its several departments? In the case of new company, the commissioner does all of those things. (See Chief Justice Gibson's opinion in *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal. 2d 344, 356 [139 P. 2d 908].)

New company would have no existence had it not been for the technical insolvency of old company. No new money constituted the assets of new company which was organized with the assets of old company. If new company were a solvent independent and distinct corporation, the insurance commissioner would not be holding its stock for the policyholders of old company. The stockholders of new company would be holding their own stock supported by assets in the hands of the officers and directors of the company. Section 11525 provides that "A solvent domestic incorporated insurer [is one] having a paid-in capital represented by outstanding shares of capital stock and issuing, on a reserve basis, nonassessable policies of life insurance or of both life and disability insurance. . . ." Surely in the normal case, "outstanding shares of capital stock" refers to stock held by stockholders, *not* by the commissioner!

Mr. Justice Traynor has pointed out how the use of the solvent mutualization procedure has deprived the members of old company of their right to the protection of court scrutiny of the plan of mutualization. He shows how the procedure used here cannot apply to the facts of the case because in the ordinary case of a voluntary mutualization, the shareholders would have the power to protect their interests by withholding their consent to the plan of mutualization. The sections of the code which relate to mutualization of insolvent companies were clearly intended by

the Legislature to protect the interests of the interested parties by providing for court approval.

In the present case by the use of the procedure provided for in the case of a solvent company, the commissioner approves a plan to be formulated in the future. When that plan is formulated, as holder of all the stock, he votes for the plan. Then, as commissioner, he approves the plan as fair and equitable. We are told by the majority opinion that "it must be assumed that the Legislature realized that the commissioner might be required to pass upon the fairness of a plan in a case where he, acting as conservator, had previously consented to mutualization on behalf of the stockholders." Nothing of the kind must be assumed. It is obvious from even a casual reading of the code provisions relating to insolvent companies (1043 et seq.) and those relating to solvent companies (11525 et seq.) that the Legislature had not the faintest thought that the two would be so commingled as they are in this case, or that the commissioner would be placed in a position where he was forced to approve a plan to be formulated some 10 years in the future, then, when the plan was formulated forced to vote an approval of it as a sole stockholder, and still later, to give his approval of something he had theretofore twice before approved.

Ever since the inception* of the receivership proceedings and the organization of new company all the parties and proceedings concerned in the rehabilitation matter have been subject to the continuing jurisdiction and supervision of the court. It has been pointed out in various phases of this litigation that new company was organized by the commissioner as his *corporate agent* to rehabilitate the business of old company. Without the original proceeding under section 1011 (d) of the Insurance Code, new company would not have come into being.

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*(With the exception of the present proceeding to be hereinafter discussed.)

It is necessary, next, to note the difference in methods provided for in the two divisions of the Insurance Code for mutualization of insolvent and solvent companies.

Section 1046 provides that "Said mutualization plan [called involuntary mutualization for insolvent companies and follows the section (1045) which provides: "If *at any time after the issuance of an order under section 1011*" the *"commissioner"* shall formulate a plan of mutualization] *shall* include provisions for:

"(a) [Acquisition of capital stock.] The acquisition by such insurer of all outstanding shares of its capital stock at a price and upon terms and conditions to be fixed as hereinafter provided.

"(b) [Retirement of capital stock.] The retirement of said shares of stock when acquired by such insurer.

"(c) [Amendment of charter.] The amendment of the charter of such insurer so as to enable it to transact its business as a mutual insurer issuing nonassessable policies on a reserve basis.

"(d) [Payment of claims.] The manner in which and the time within which, after mutualization is effected, matured and maturing claims against such insurer shall be paid to the lawful holders thereof.

"(e) [Submission of plan to policyholders.] The submission of said mutualization plan to the policyholders of such insurer under such procedure as shall be set forth in the plan or prescribed by said court, for their approval or rejection.

"(f) [Notice to shareholders.] Notice to the shareholders of such insurer, in such manner and at such time after the approval of said mutualization plan by said policyholders, as the court may direct."

Section 1048 provides that after the formulation of the mutualization plan, the commissioner shall submit it to the court for its order directing the submission thereof to the policyholders named in subdivision (e), of section 1046.

Section 11526 (relating to *solvent* insurers) provides that "Such plan shall include appropriate proceedings for amending the insurer's articles of incorporation to give effect to the acquisition, by said insurer, for the benefit of its policy holders or any class or classes thereof, of the outstanding shares of its capital stock and the conversion of the insurer from a stock corporation into a nonstock corporation for the benefit of its members. The members of such nonstock corporation shall be the policyholders from time to time of the class or classes for whose benefit the stock of the insurer was acquired, and no other persons. Such plan shall be:

"(a) Adopted by a vote of a majority of the directors. [As distinguished from the formation thereof by the commissioner as provided in section 1045.]

"(b) Approved by the vote of the holders of at least a majority of the outstanding shares at a special meeting of *shareholders* called for that purpose, or by the written consent of such shareholders. [As distinguished from section 1048 requiring the commissioner to obtain court approval and an order of the court directing the submission of the plan to the policyholders.]

"(c) Submitted to the commissioner and approved by him in writing. [Under the circumstances here prevailing with regard to the commissioner's position as conservator, liquidator and general supervisor of new company, this amounts to an idle act.]

"(d) Approved by a majority vote of all the *policyholders* of the class or classes for whose benefit the stock

is to be acquired voting at an election by the policyholders called for that purpose, subject to the provisions of section 11528. . . .

(e) Filed in the office of the Insurance Commissioner after having been approved as provided in subdivisions (b), (c) and (d) of this section."

Under the provisions of the rehabilitation agreement, a price determination committee consisting of four members was set up. The price determination committee reported to new company, in April, 1950, that mutualization was practicable and valued the stock of new company at $3,000,000. The mutualization plan provided in part for the payment of the purchase price with simple interest at the rate of long term government bonds (2½%). Under the terms of the rehabilitation agreement, "The Conservator for himself and for any successors in the ownership of said stock claiming under him in any manner other than through a sale of said stock pursuant to the provisions of subparagraph (d) hereof agrees to consent and hereby consents as the holder and owner of the stock of the New Company to such plan of mutualization. In the event said mutualization plan is adopted, the Conservator, or a Liquidator as aforesaid, shall dispose of such stock in accordance with such plan."

Under the voluntary mutualization procedure heretofore set forth (section 11526) the mutualization plan is submitted to the commissioner after adoption by a vote of a majority of the directors and after a vote by a majority of the outstanding shares at a special meeting of shareholders called for that purpose. Section 11527 provides that "The Commissioner shall examine the plan submitted to him under the provisions of subdivision (c) of section 11526. *He shall not approve such plan unless in his opinion*

the rights and interests of the insurer, its policyholders and shareholders are protected nor unless he is satisfied that the plan will be fair and equitable in its operation." (Emphasis added.) Fair and equitable to *which* company?

Under the provision of the rehabilitation agreement heretofore set forth, the then commissioner agreed for himself, and his successors, to agree to any plan promulgated by the price determination committee. It should be borne in mind that the stock of new company is now held by voting trustees who had no discretion, but were (as stated in the insurance commissioner's answering brief, p. 73) "not only *authorized,* but *bound* to give their consent; and [that] they had no discretion to exercise." (Emphasis that of the commissioner.) There is evidence in the record which shows that the trustees voted for the plan of mutualization because they were told to so vote; that they did not examine into the merits of the plan. The next step provided for in section 11526 (Ins. Code) is that the plan shall be submitted to the commissioner for his written approval. The insurance commissioner states (Answering brief, p. 83), "As we have already shown, the Liquidator [commissioner] has bound himself to consent to a Plan of Mutualization proposed in accordance with the Rehabilitation Agreement." The code, however, (§ 11527) provides that the commissioner shall examine the plan submitted to him under the provisions of subdivision (c) of section 11526 and that *"He shall not approve such plan unless in his opinion the rights and interests of the insurer, its policyholders and shareholders are protected nor unless he is satisfied that the plan will be fair and equitable in its operation."* (Emphasis added.) The net result, under the circumstances prevailing in this case, is that the commissioner, as beneficial owner of all the stock of the new company, instructs the voting trustees to vote for any plan proposed by the price determination committee and then, when such plan is submitted

to him for his approval, places his rubber stamp of approval thereon because he (or his predecessor) has, 10 years prior to the promulgation of the plan, agreed to approve it *no matter what it is*—agreed, not only for himself, but for any successor in office, to approve the plan as proposed. It is shown, therefore, without a shadow of a doubt, that the earlier agreement to approve any plan proposed by the price determination committee has the effect of nullifying section 11527 of the Insurance Code, as well as the sections relating to mutualization of insolvent insurers.

Had the procedure outlined in sections 1045, 1046 and 1048 been followed, the result would be very different. Under section 1045 the *commissioner* would formulate the mutualization plan for the purpose of carrying out the rehabilitation of the insurer whose business was seized under the provisions of section 1011. The commissioner's plan would then be submitted to the court for its order directing the submission of the mutualization plan to the shareholders and policyholders of the seized insurer for their vote of approval, or disapproval as the case might be (§ 1046, subds. (e) and (f)). Old company, not having been dissolved, still exists; new company was organized as the corporate agent of the commissioner to rehabilitate the business of old company with the assets of old company. New company cannot, as it appears, be considered as a completely independent and solvent organization under the facts here prevailing. As I have pointed out, the commissioner holds the entire beneficial interest in all the capital stock of new company for the benefit of stockholders, policyholders and creditors of old company; the legal title to the stock of new company is held by voting trustees who vote it as directed by the commissioner. As I have also pointed out, the board of directors of new company are under the close supervision, control and direction of the commissioner and must, in reality, take orders from him as to every major,

and some minor, business details. It cannot be said that this close supervision, control and direction exist in the usual "solvent" corporation.

Corporate Entity of New Company

Respondents argue that the corporate entity of new company cannot be disregarded so as to make the proposed mutualization a mutualization of old company. In support of this contention, *In re Bond & Mort. Guar. Corp.* 157 Misc. 240 [283 N.Y.S. 623, 652], and *Garrison* v. *Pacific Mut. L. Ins. Co.,* 83 Cal.App.2d 1, 9-10 [187 P.2d 893], are cited. In neither case was mutualization involved. In the Bond & Mortgage Guarantee case, the superintendent of insurance had organized Bond & Mortgage Guarantee *Corporation* "as a domestic insurance corporation, with a capital of $1,000,000, a surplus of $2,000,000, and a reserve for contingencies of $200,000, all of which was paid out of the assets of the guarantee *company* in exchange for the entire capital stock of the new corporation, 10,000 shares of the par value of $100 each; a certificate for said number of shares was issued in the name of the guarantee *company* and is held by the superintendent of insurance as an asset, for the benefit of the creditors (including the policyholders), of the guarantee *company.*" (Emphasis added.) The guarantee corporation here involved took on the duty of insuring mortgages, "but on a restricted basis under a limited policy of guaranty." (Pp. 641, 650.) This case involved a proceeding whereby the People, and certain individuals interested, applied for an order enjoining the State Mortgage Commission from demanding and receiving or assuming control of certain mortgages being serviced by the guarantee *corporation* pursuant to court order. The injunction was granted. The contention was that the guarantee corporation, in servicing mortgages, was acting with-

out adequate corporate powers. The court held that the corporation was acting within its corporate authority and, in answer to the contention that the guarantee corporation was a state agency inseparable from the superintendent of insurance (so as to permit another state agency, the Mortgage Commission, which came into being *after* the proceedings set forth had been had) to take it over, the court said: "Said corporation is like any other corporation; a distinct entity. All of its stock is owned by guarantee *company,* and the certificate therefor is held in the custody of the superintendent; this he holds as he does any other assets of the company in rehabilitation, as a receiver designated by statute for the benefit of the creditors and stockholders of said company; not as an owner, representing the state. It is a stock corporation, having been created, for one thing, *with a view to its possible sale for the benefit of the creditors, as its exhaustive by-laws make apparent.* During such time as the stock control remains as it is, the operation of the corporation is to be under the supervision of the superintendent as rehabilitator." (Emphasis added.) The court continued and said that the primary management of the corporation was with the board of directors, although it was subject to the supervision of the superintendent "in his capacity as supervisor of insurance companies" (pp. 651, 652). The situation presented in the New York case and that presented in the case at bar are factually similar up to a point. I have heretofore quoted extensively from *Caminetti* v. *Pacific Mut. L. Ins. Co.,* 22 Cal.2d 344, at page 356 [139 P.2d 908], wherein we set forth the extensive and minute supervision exercised by the commissioner over new company. This supervision exceeded by far anything required of him as "supervisor of insurance companies." We also said in *Carpenter* v. *Pacific Mut. L. Ins. Co.,* 10 Cal.2d 307, 324, 325 [74 P.2d 761], that new company was organized "as a corporate agent to assist him [commis-

sioner] in carrying on the business of the old company." (See also *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 77, 80 [136 P.2d 779].)

In *Garrison* v. *Pacific Mut. L. Ins. Co.*, 83 Cal.App.2d 1 [187 P.2d 893], the court said, "The question for decision is whether an insurance company which was organized to conserve an insolvent insurance company and to rehabilitate its business is obligated to pay interest on claims allowed by the conservator against such insolvent, based upon the breach by the latter of certain policies, in the absence from the rehabilitation agreement of a specific promise to pay such interest, the agreement having provided for the payment to the liquidator for the benefit of such claimants an amount equal to the sum of all 'allowed claims' against the insolvent company." New company, by the terms of the rehabilitation agreement had agreed (Paragraph 17) "to pay to the liquidator for payment to claimants an amount equal to the sum of all claims against old company filed with the liquidator and finally allowed." The court answered the question put with this statement: "It is customary practice in liquidation proceedings to marshal the assets of the debtor, fix the amount of its liabilities and disburse the assets among the creditors pro rata. Such a process would not be possible, if during the season of liquidation, the claims should be varied by the additions of varying amounts of interest." (P. 9.) Respondents rely upon the following paragraph from the opinion of the District Court in the Garrison case: "Appellants contend that new company is a reincarnation of old company and, therefore, has impliedly promised to pay all of the latter's indebtedness. In this they ignore provisions of the Insurance Code, article 14 of chapter 1, part 2, division 1, which article deals with insolvency and liquidation proceedings. Section 1043 of such article provides that in any proceeding under the article, *the commissioner may mutualize or reinsure the*

business of any person affected by proceedings thereunder and may enter into rehabilitation agreements. *New company was organized by the sovereign power for the purpose of rehabilitating the business of one of its own creatures whose very existence inhered in the blood and sweat of the people.* It was to go forward under the guidance of the state. Its identity is utterly distinct from that of old company, notwithstanding the latter's equitable ownership of new company's stock. It cannot be fairly said that it is a continuance of old company. It did not take over the latter's assets or assume its burdens at the behest of old company. Such transfer and assumption were rendered indispensable to the public weal and were required by law to conserve the common good in general and the army of policyholders of old company in particular. New company was not organized by old company to do service in a prescribed manner for the latter but was created by the state to perform a public service. It must be and act in its own right upon the arena of trade and commerce and of human existence, free from the fetters of a collapsed institution which in the kaleidoscope of a changing world will soon be only a memory." (Pp. 9, 10.) New company was organized by the state to rehabilitate the business of the old company; as the "corporate agent" of the insurance commissioner for that purpose. The language justed quoted is, in part, illogical under the facts presented in this long line of litigation, including the Garrison case. It appears to me that the statement that "its [new company] identity is *utterly* distinct" is inconsistent with the latter part of the same sentence that this was so "notwithstanding the latter's [old company] equitable ownership of new company's stock" and with one of the preceding sentences wherein it is said that "New company was organized by the sovereign power for the purpose of rehabilitating the business of "old company, and the fact that new company "was to go forward under

the guidance of the state." The duties and obligations imposed upon the commissioner in this case amount to far more than his usual supervision of the usual solvent insurance company. There can be no doubt that new company is a separate *corporate* agency and that it was not organized by old company, but it does not logically follow that it is "utterly distinct" from old company. In my opinion, new company would have no existence but for the insolvency proceedings against old company. It also conclusively appears that the quoted statement from the Garrison case is dictum since it had nothing to do with the question involved there.

Respondents also argue that because this court said in *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal.2d 307, 334 [74 P.2d 761], that new company was, as a reinsurer, "substituted as an insurer in the place and stead of the original insurer" that the corporate identity of new company cannot be disregarded; that because this court said in the Carpenter case (p. 335) that "Every policyholder who consents to the Plan clearly enters into a novation with the New Company" that the two companies cannot be considered as "essentially one and the same." New company will in time replace old company but so long as old company exists *in any form*, it is clear that new company is still *only the corporate agent* of the commissioner for the purpose of rehabilitating the business of old company and that the mutualization plan must be worked out in accordance with the procedure provided for in that part of the Insurance Code relating to involuntary mutualization of insolvent companies. The stock of new company, held now by voting trustees, with beneficial ownership in the commissioner is still held by him for the benefit of the policyholders and creditors of old company. This fact cannot be disregarded; nor can the rights of the policyholders and creditors of old company be disregarded. In holding that

new company is "utterly distinct" from old company for *all purposes,* a majority of this court chooses to forget *all the facts* concerning this litigation and pretends that new company was organized as any other insurance company with its own assets and liabilities, that the insurance commissioner had only the normal, nominal, supervision over its affairs, and that no insolvency proceedings had ever been involved. In the light of the record before us, such a holding cannot stand the test of honest scrutiny.

Res Judicata

Respondents argue that it has been decided by the superior court that the commissioner had authority to include in a rehabilitation agreement an option to mutualize the new company by voluntary proceedings and to agree to dispose of the stock of new company at the price, and on the terms, fixed by the price determination committee; and that this court has decided that the superior court had jurisdiction to so decide and that the superior court did not abuse its discretion in approving the rehabilitation agreement.

In the commissioner's answering brief (p. 61) is found this statement: "It is true that no attack seems to have been made on the mutualization provisions [of the rehabilitation agreement] in any of the appellate proceedings, but the courts have taken notice of them in determining various appeals." Neither this court, nor an appellate court, has been concerned in any of this litigation with the mutualization provisions of the rehabilitation agreement as will hereinafter appear.

In *Carpenter* v. *Pacific Mut. L. Ins. Co.,* 10 Cal.2d 307, 322 [74 P.2d 761], we said that the plan of rehabilitation provided for "Ultimate mutualization, in the event the policyholders so elect." We were there concerned in the main with the organization of new company as the corporate

agent of the commissioner to rehabilitate the business of old company. In *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 13 Cal.2d 306 [89 P.2d 637], we were concerned with the validity of the "Order for Liquidation" and the mutualization provisions of the plan were not considered. In *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 14 Cal. 2d 704 [96 P. 2d 796], we were concerned with an order of the trial court correcting its minutes, *nunc pro tunc*. In *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 77 [136 P.2d 779], we were concerned with the claims of dissenting policyholders and, once again, the mutualization provisions were not considered. In *Caminetti* v. *Pacific Mut L. Ins Co.*, 22 Cal. 2d 344, 353 [139 P.2d 908], we were concerned with the propriety of creating a voting trust with the stock of new company under the provisions of section 1037, subdivision (e), of the Insurance Code. We said there that "To adopt the contention that section 1037(e) was not intended to apply to stock of an insurance company *organized as a medium through which rehabilitation of the business of a delinquent insurer was to be accomplished would require us to disregard the clear language of the statute.* Section 1037(e) specifically refers to stock issued to the commissioner 'as conservator or as liquidator in connection with a rehabilitation or reinsurance agreement.'" (Emphasis added.) We also said there (p. 355) that the rehabilitation agreement (Paragraph 20) related to the "ultimate status and ownership of the new company." We then pointed out that subdivision (a) (Paragraph 20) authorizes the commissioner to dispose of the stock in accordance with "any plan of mutualization thereafter adopted by the policyholders of the new company, and such a disposition may include a transfer to voting trustees if the plan of mutualization so provides." We held that the voting trust agreement was not a disposal of the stock within the meaning or purpose of Paragraph 20 of the rehabilitation agreement and we said (p. 358) that "It

is true that the words 'dispose of' are used in subdivision (a) of paragraph 20 in connection with an authorization to the commissioner to transfer the stock of the new company to voting trustees in accordance with a plan of mutualization. *But it is clear that under that subdivision the transfer there provided for would require a complete alienation of the stock in order* to carry out the plan of mutualization contemplated therein." (Emphasis added.) Again, the validity of the mutualization procedure was not passed upon; the only holding being that the rehabilitation agreement did not preclude the creation of the voting trust. In *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 386 [139 P.2d 930], we were concerned with disqualification of a judge and a party's waiver thereof. Mutualization was not considered. In *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 23 Cal.2d 94 [142 P.2d 741], we were concerned with the correctness of the measure of damages adopted by the commissioner to be allowed disability policyholders. In *Garrison* v. *Pacific Mut. L. Ins. Co.*, 83 Cal.App.2d 1 [187 P.2d 893], the court was concerned with the question of interest on claims allowed by the commissioner. In *Sanborn* v. *Pacific Mut. L. Ins. Co.*, 42 Cal.App.2d 99 [108 P.2d 458], the court pointed out that the following questions were involved: What was the effective date of the agreement between new company and the insurance commissioner as conservator of old company? Did appellant's present disability commence prior to such date and was notice of claim filed in accordance with the agreement?

It is contended by respondents, however, that a judgment upholding the validity of a contract establishes its validity, not only against the attacks actually made, but against those that could have been made, even though no question of invalidity was raised in the original proceeding and even though the judgment does not expressly pass on the contract.

Appellants argue that the procedure for mutualization provided for by statute cannot be altered by contract and that any attempt to do so is against public policy, illegal and void. It is true, of course, that the plan of mutualization, as proposed by the price determination committee, has never been before the courts until the present proceeding. The trial court, in its order of December 4, 1936, stated (13) "That said Rehabilitation and Reinsurance Agreement, and each and all of the terms and conditions thereof, and the plan therein embodied are, and each of them is, hereby approved; . . ." (Clk. Tr. p. 169.) This was an approval *only* of the agreement and, while grossly wrong, does not now preclude this court from correcting the error since the *plan* of *mutualization* was not passed upon *nor could it have been* since it was to be promulgated *10* years in the future.

We said in the Caminetti case (22 Cal.2d 344, 363) "This proceeding is wholly statutory. The duties imposed upon the commissioner, and the supervision over him vested in the courts, result from the statute." Appellants, citing *Fortenbury* v. *Superior Court,* 16 Cal.2d 405, 407-408 [106 P.2d 411], contend that if the order of the trial court (December 4, 1936) is considered as having approved a plan of mutualization contrary to the statutory provisions therefor, it is void for want of jurisdiction of the subject matter. The respondents' position is that this court having previously determined the trial court's jurisdiction, the matter is res judicata. In the Fortenbury case, we said "The term jurisdiction originally included only the right to hear and determine concerning the subject matter in a particular case. But the modern tendency has been to broaden the meaning, particularly where the right to review a decision by certiorari, or other prerogative writ is the question for decision. *A court may have jurisdiction of the cause of action and of the parties, but it may lack the authority or power to act in the case except in a particular way.* Under

such circumstances, it is now generally held that the court had no jurisdiction. As pointed out in the case of *Spreckels S. Co.* v. *Industrial Acc. Com.*, 186 Cal. 256, 260 [199 P. 8], 'the word is frequently used as meaning authority to do the particular thing done, or, putting it conversely, a want of jurisdiction frequently means a want of authority to exercise in a particular manner a power which the board or tribunal has, the doing in excess of the authority possessed.' " (Emphasis added.) We also said in *First Industrial Loan Co.* v. *Daugherty*, 26 Cal.2d 545, 556 [159 P.2d 921], that "It is elementary that power given to the Commissioner of Corporations (by section 10 of the act) 'to establish such rules and regulations as may be reasonable or necessary to carry out the purposes and provisions of this act' *does not include power to alter the statute or enlarge or impair its scope.*" (Emphasis added.)

It seems apparent that if the involuntary mutualization provisions for insolvent insurance companies are applicable the commissioner was acting without statutory authority in approving a plan of mutualization based upon the statutory provisions relating to voluntary mutualization of solvent companies and that his approval thereof was void, as was his agreement to approve such a plan. The rule is settled that a contract in violation of an express statutory provision is void and that it is not necessary that the statute expressly so declare (*City of Oakland* v. *California Const. Co.*, 15 Cal.2d 573, 576 [104 P.2d 30]). A contract made in any manner except that expressly provided in the applicable statute is ipso facto void (*Dale* v. *Palmer*, 106 Cal. App. 2d 663, 667 [235 P.2d 650]). If upon review of all the legislation on the subject the contract appears to contravene the design and policy of the laws, the courts will not enforce it (*Kreamer* v. *Earl*, 91 Cal. 112 [27 P. 735]; *Loew's Inc.* v. *Cole*, 185 F.2d 641). See *Hill* v. *Bank of San Pedro*, 41 Cal. App. 2d 595, 607 [107 P.2d 399]; *County of San Diego*

v. *California Water etc. Co.*, 30 Cal.2d 817 [186 P.2d 124, 175 A.L.R. 747]; *Film Producers, Inc.* v. *Jordan*, 171 Cal. 664 [154 P. 605].

The parties are in disagreement as to whether or not the mutualization provisions were litigated at the time the order of December 4, 1936, was made. The insurance commissioner says that "*Presumably* these provisions did not go entirely unchallenged in the proceedings leading up to the Order of Rehabilitation." (Emphasis added.) (Insurance commissioner's answering brief, p. 61.) New company asserts that the "validity" of the rehabilitation agreement was put in issue and decided by the order of December 4, 1936, and that the same has been approved by this court. From all that appears, it is obvious that the precise question here involved has never been passed upon. It most certainly has not been passed upon by an appellate court, or by this court. Respondent, new company, points to the following quotations from the pleadings in the original proceeding as showing that the mutualization provisions of paragraph 20(a) were litigated. "Answer of Certain Interveners to Petition for Approval of Second Proposed Rehabilitation and Reinsurance Agreement, Folios 2757-2759 of Transcript on Appeal. L. A. 16182:

"That said plan, if executed, would be entirely void and of no effect, and would not be binding upon the parties thereto, and that the execution of the same is beyond the authority of the said Samuel L. Carpenter, Jr., as Insurance Commissioner of the State of California and as Conservator of The Pacific Mutual Life Insurance Company of California [old company], and that the execution of said agreement and the transfer of the assets by the said Insurance Commissioner is wholly unauthorized by the Insurance Code of the state of California and is entirely beyond the power of the said Samuel L. Carpenter, Jr., as Insurance Commissioner and as Conservator as aforesaid, and the said

agreement will be void when executed and beyond the power of the Insurance Commissioner under the statute in such cases made and provided and that the said agreement is of no binding effect whatever on any of the parties thereto and that any acts done pursuant thereto are wholly null and void."

"Amended Complaint in Intervention of Certain Intervenors, Folio 3882 of Transcript on Appeal, L. A. 16182:

"That the approval of said agreement is beyond the authority and jurisdiction of this court and, if given, would be void and of no force and effect, for the reason that authority therefor is not given in, and, in fact, is forbidden by, the terms and provisions of said Insurance Code of California, and, in particular, of articles is [sic] and 14 of chapter 1 of part 2 of division 1 thereof."

It appears to me that what was undoubtedly meant by these pleadings was that the *organization* of *new company* was said to be beyond the commissioner's power since that was the major issue in *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal.2d 307 [74 P.2d 761].

The next question that arises is whether or not the provisions for mutualization *could* have been litigated in that proceeding inasmuch as mutualization was not to take place until between 1946 and 1948, or "so long as the Conservator or a Liquidator of the Old Company may continue to hold any or all of said stock. . . ." (Paragraph 20(a), rehabilitation agreement.) The proposed voluntary mutualization plan was also to be in accordance "with the laws of the State of California in effect at the time of said request. . . ." The plan was also not to be proposed unless the price determination committee "shall determine whether in their opinion the proposed voluntary mutualization of the New Company . . . can then be practicably accomplished. . . ." In *Silva* v. *City & County of San Francisco*, 87 Cal.App.2d 784 [198 P.2d 78], a county board of supervisors passed a resolution

that certain land of plaintiff's should be acquired when necessary. Plaintiff sued for a declaration as to the value of his property. The court, in refusing to place plaintiff's valuation on the property, declared: "The court may take judicial knowledge that real estate values do not remain constant. The value fixed during the present period may be disproportionate to what should be paid when the recreation department of the city decides to use the property as part of a 'playground.' Plaintiff seeks a final determination that the property is worth $10,000 and that *if* and *when* defendant chooses to take the property this will be the amount it must pay." (Emphasis that of the court.) It was also said that ". . . the present complaint alleges in substance that the value of the property may be determined through condemnation proceedings when defendant deems it 'necessary.' The only declaratory judgment that could be rendered under the allegations of the complaint would be of an advisory nature—namely, that when defendant deems it necessary to institute condemnation proceedings the price be fixed at the then market value." (Pp. 788-789.)

In *Young* v. *Young,* 100 Cal.App.2d 85, 87 [223 P.2d 25], it was held that an action to establish a foreign decree of divorce in California, and for ratification by the California court of a property settlement included in the foreign decree, did not present a justiciable controversy in the absence of a showing that defendant had refused or failed to comply with the foreign decree or the terms of the property settlement agreement. It was held that "The rule is accurately stated in 1 California Jurisprudence (1921) at page 335, section 25, as follows: 'To invoke the jurisdiction of a court of justice, it is primarily essential that there be involved a genuine and existing controversy, calling for present adjudication as involving present rights.' (See also *Neill* v. *Five C. Refining Co.,* 79 Cal.App.2d 191 [179P.2d 818]), wherein Mr. Justice Drapeau thus pointedly

states the rule at page 193, 'An action not founded upon an actual controversy, or prosecuted "for the gratification of the curiosity of the litigants" is collusive and will not be entertained. [Citing cases.]' "

In *Merkley* v. *Merkley,* 12 Cal.2d 543, 547 [86 P.2d 89], the court stated that "The facts in the record present an academic question only. The courts will not exercise the discretionary power to declare rights which do not give rise to a present controversy."

In *County of San Diego* v. *California Water etc. Co.,* 30 Cal.2d 817, 823, 826 [186 P.2d 124, 175 A.L.R. 747], a case involving an agreement by a county to relocate a county highway, we enunciated the following rule: That if the Legislature had provided a method by which a county or city might abandon or vacate roads, that method was *exclusive.* We said: "It is clear, however, that neither the doctrine of estoppel nor any other equitable principle may be invoked against a governmental body where it would operate to defeat the effective operation of a policy adopted to protect the public. (See *Miller* v. *McKinnon,* 20 Cal.2d 83 [124 P.2d 34, 140 A.L.R. 570], and cases cited therein; *Pan Amer. Co.* v. *United States,* 273 U.S. 456, 505-506 [47 S.Ct. 416, 71 L.Ed. 734]; *American Surety Co. of N. Y.* v. *United States* (C.C.A. 10th), 112 F.2d 903, 906.) In the American Surety Company case the court stated that the government could not be estopped so as to 'frustrate the purpose of its laws or thwart its public policy.' (112 F.2d, at p. 906.) In 3 McQuillin, Municipal Corporations [2d ed., 1943], section 1266, it is said that various statutory procedures or steps exist to protect citizens and taxpayers from ill-considered contracts or those showing favoritism and that if recovery is allowed for property or services on the ground of estoppel or implied contract, 'then it follows as the night the day that the statute or charter provision can always be evaded and set at

naught.' The author adds that the rule denying indirect enforcement of such void contracts harmonizes with our governmental system, appears to be supported by reason, and is not unjust, because the other party is charged with notice of the law."

At any rate, the *plan* of mutualization, as distinguished from the *provisions* for mutualization as found in the rehabilitation agreement, has never until this case, been passed upon. That plan, while following the outline contained in Paragraph 20(a) made some 10 years prior to the promulgation of the one here under consideration, is an entirely different matter and may properly be held void as not in accordance with the statutory scheme for involuntary mutualization of insolvent insurance companies seized by the commissioner under the provisions of sections 1010 and 1011 of the Insurance Code. The rule enunciated in *County of San Diego* v. *California Water etc. Co., supra,* hereinabove set forth would be applicable if the plan of mutualization is held void as against public policy and as being in excess of the commissioner's jurisdiction.

It should be noted that Paragraph 20(f) contains a provision to the effect that if all, or any part, of the paragraph should be contrary to law, or illegal, or void, the vulnerable provision should be deemed separable and the balance of the agreement should stand. If, as I believe, the validity of Paragraph 20(a) has never been before determined, the provision just noted would prevent anything that has been heretofore determined by either this court, or any appellate court, from conflicting with the determination made here.

Trial De Novo

If the procedure for involuntary mutualization had been followed, as it should have been, this question would

never have arisen. Section 1048 of the Insurance Code provides that after the formulation of the mutualization plan, it "shall" be submitted by the commissioner to the court for its approval. The clear import of the procedure outlined for insolvent organizations is that those possessed of property rights in them must be accorded *court* protection at *every* stage. For example, the *court* appoints the appraisers (§ 1051.) Such court approval, required by section 1048, accords the interested parties the equivalent of a trial de novo.

According to the majority opinion, the "alternative" reason given for affirmance is reliance upon the doctrine of res judicata. That this reason is patently false is shown by Mr. Justice Traynor when he points out that the court "could obviously not approve [the] plan at the time it entered its order approving the rehabilitation agreement. Moreover, it did not expressly approve in advance the carrying out of any mutualization plan that might be presented by the price determination committee." He shows that there is reserved to the court, by the agreement, continuing jurisdiction to approve or disapprove plans to be developed in the future for mutualization or other disposal of the stock in the hands of the commissioner. He points out that to so interpret the order subserves the primary purpose of section 1037, subdivision (d), of the Insurance Code by securing to all interested parties "their right to court scrutiny." Appellants have not been accorded "court scrutiny" in its true sense.

Appellants correctly contend that the order of the commissioner approving the plan of mutualization was subject to full judicial review by the superior court. It is argued that the commissioner, in making his order, acted in a judicial capacity rather than in an administrative or legislative capacity as contended by respondents. Appellants contend that in reviewing a decision or order of a statewide

administrative agency or of a state officer, the superior court must reweigh the evidence and determine for itself according to its independent judgment whether or not the decision is supported by the weight or preponderance of the evidence in every case where state judicial functions are involved. They rely upon *Thomas* v. *California Emp. Stab. Com.*, 39 Cal.2d 501, 504 [247 P.2d 561]; *Moran* v. *Board of Medical Examiners*, 32 Cal.2d 301, 308 [196 P. 2d 20]; *Laisne* v. *California State Board of Optometry*, 19 Cal.2d 831, 834-835 [123 P.2d 457]; and *Drummey* v. *State Board of Funeral Directors & Embalmers*, 13 Cal.2d 75 [87 P.2d 848]. Respondents, on the other hand, argue that the commissioner's order was an exercise of executive power and was not the exercise of such full judicial power as to entitle appellants to have the trial court exercise its independent judgment with respect to the weight of the evidence. Respondents rely upon the cases of *Bank of Italy* v. *Johnson*, 200 Cal. 1 [251 P. 784]; *Doble Steam Motors Corp.* v. *Daugherty*, 195 Cal. 158 [232 P. 140]; *McDonough* v. *Goodcell*, 13 Cal.2d 741 [91 P.2d 1035, 123 A.L.R. 1205], and *Southern Calif. Jockey Club, Inc.* v. *California etc. Racing Board*, 36 Cal.2d 167 [223 P.2d 1].

The duties of the commissioner, as set forth in section 12921 have been held to be "that of a minister of the court in possession of the property, to the end of conserving the rights of everybody having any interest" (*H. D. Roosen Co.* v. *Pacific Radio Pub. Co.*, 123 Cal. App. 525 [11 P.2d 873]) and discretionary (*Garris* v. *Carpenter*, 33 Cal. App.2d 649, 657 [92 P.2d 688]). It was held in *Caminetti* v. *Guaranty Union Life Ins. Co.*, 22 Cal.2d 759, 764 [141 P.2d 423], that the commissioner's ". . . office is not to perform functions in aid of the court's jurisdiction to decide a controversy between litigants, but he acts as a statutory officer, subject however to judicial supervision to prevent an arbitrary exercise of power or neglect of duty." The

court in the Caminetti case, however, was referring to the commissioner as a receiver of the assets of insurance companies and stated that he did not derive his power from the court, but from the statute.

The distinction in the two lines of cases relied upon by appellants and respondents is that in those relied upon by appellants an existing vested property right was extinguished, or taken away, by the administrative order. For example, in the Drummey case (13 Cal.2d 75) Drummey and Wilson had been duly licensed embalmers and the State Board of Funeral Directors and Embalmers ordered their licenses suspended. This court held that it was dealing with a statute which conferred certain fact-finding powers on a board exercising statewide jurisdiction and that there was no "indication that the legislature intended the facts so found to be binding on the courts"; that no method of review was provided in the statute. We held that we could see no escape from the conclusion that in such a proceeding the court to which the application for mandate is made must weigh the evidence, and exercise its independent judgment on the facts as well as the law, if the complaining party is to be accorded his constitutional rights under the state and federal Constitutions. "The state constitutional provision discussed, *supra,* prohibits the conferring of judicial power on such administrative boards" (p. 84).

In *Laisne* v. *California State Board of Optometry, supra,* the California State Board of Optometry had revoked Laisne's certificate of registration to practice optometry in this state. We held there that "On the authority of the Drummey case the only type of review that would afford appellant his full constitutional rights would be a complete trial de novo as outlined in the decision in that case." (P. 843.)

In *Moran* v. *Board of Medical Examiners, supra,* the State Board of Medical Examiners revoked the license of

Dr. Moran to practice medicine in this state. We held "That the trial court in this case was 'authorized by law to exercise its independent judgment on the evidence' is well established. (See *Dare* v. *Board of Medical Examiners* (1943), 21 Cal.2d 790, 795 [136 P.2d 304]; *Sipper* v. *Urban* (1943), 22 Cal. 2d 138, 141 [137 P.2d 425]; *Hohreiter* v. *Garrison* (1947), 81 Cal.App.2d 384, 402 [184 P.2d 323].) As stated in the last cited case, at page 402, 'Thus, the ultimate power of decision rests with the trial court.'" (P. 308.)

In *Thomas* v. *California Emp. Stab. Com.,* 39 Cal.2d 501 [247 P.2d 561], it was held that unemployment benefits provided for by the Unemployment Insurance Act were such property rights as to fall within the rule that persons deprived of property rights by a statutory administrative agency were entitled to a limited trial de novo in the superior court.

Respondents' position (which has been adopted in toto by the majority opinion) is that the "Order" of the commissioner was merely a "permit" which allowed mutualization if the policyholders so voted (§ 11526, subd. (d)) and that the order did not deprive anyone of vested property rights. We have heretofore held (*Thomas* v. *California Emp. Stab. Com.,* 39 Cal.2d 501, 504 [247 P.2d 561]; *Laisne* v. *California State Board of Optometry,* 19 Cal.2d 831 [123 P.2d 457]; *Moran* v. *Board of Medical Examiners,* 32 Cal.2d 301, 308 [196 P.2d 20]; *Drummey* v. *State Board of Funeral Directors & Embalmers,* 13 Cal.2d 75 [87 P.2d 848]) that where an existing property right is extinguished by the questioned administrative order the one so deprived is entitled to a trial de novo in the superior court. Appellants here are the beneficial owners of the stock of the new company which is held by the voting trustees for their benefit. Under the proposed mutualization plan, this stock will be nonexistent and they will be forced to accept a price therefor, as well as terms,

over which they have exercised no control. Mr. Justice Traynor has pointed out that if the proper procedure had been followed, the rights of these people would have been protected by a court of law, rather than subjected to the action of one man acting in three irreconcilable positions. The assets of old company were transferred to new company in exchange for all the stock of new company which, in the beginning, was held by the commissioner, as conservator for the benefit of the creditors, policyholders, and stockholders of old company (*Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 344, 351 [139 P.2d 908]). Later, the stock of new company was transferred to voting trustees who held legal title thereto, ". . . with the power to exercise all the rights of ownership. The commissioner, however, retains the entire beneficial interest for the benefit of creditors of the old company and others interested." (22 Cal.2d, at page 357.) As stated by the insurance commissioner in his opinion and decision (page 7 of the exhibit): "Greatly epitomized, the plan [of mutualization] determined that both the Participating and Non-Participating Life Departments of the company should be mutualized by the *purchase and cancellation of all of the outstanding shares of capital stock of the New Company,* thus converting the New Company into a non-stock insurer conducted for the benefit of its members who shall be the policyholders of the participating and non-participating life classes." Inasmuch as purchase and cancellation of the stock of new company will be accomplished by the proposed mutualization, it appears that appellants have been deprived, by the order, of their vested beneficial ownership of that stock so as to entitle them to a trial de novo within the rule of the cited cases.

The majority opinion states: "The approval of the mutualization plan by the commissioner did not involve any deprivation of property rights or vested rights; it was in essence a permit or license authorizing the new company

to purchase its own stock." This *would* be true *if* new company members owned their own stock (and therein lies the fallacy in calling new company a solvent corporation with all that term connotes). But the matter is not quite so simple. All the beneficial ownership, which is the *real* ownership is held by the policyholders and stockhold of old company; all the legal title is held by the voting trustees (appointed by the commissioner) for the benefit of *old company* policyholders and stockholders. In other words, new company holds neither legal nor beneficial ownership of its stock, but through the medium of the mutualization plan is given the right to deprive the beneficial owners of their property in clear violation of the law as heretofore propounded by this court. We held in the Drummey case that we could see no escape from the conclusion that the court must weigh the evidence and exercise its independent judgment on the facts as well as the law, if the complaining party was to be accorded his *constitutional rights* under the state and federal Constitutions. "The state constitutional provision discussed, *supra,* prohibits the conferring of judicial power on such administrative boards."

In *St. Joseph Stock Yards Co.* v. *United States,* 298 U.S. 38, 52 [56 S.Ct. 720, 80 L.Ed. 1033], the court stated: "Legislative agencies, with varying qualifications, work in a field peculiarly exposed to political demands. Some may be expert and impartial, others subservient. It is not difficult for them to observe the requirements of law in giving a hearing and receiving evidence. But to say that their findings of fact may be made conclusive *where constitutional rights of liberty and property are involved,* although the evidence clearly establishes that the findings are wrong and *constitutional rights have been invaded,* is to place those rights at the mercy of administrative officials and seriously to impair the security inherent in our judicial safeguards. That prospect, with our multiplication of administrative agencies, is not one to be lightly regarded.

It is said that we can retain judicial authority to examine the weight of evidence when the question concerns the right of personal liberty. But if this be so, it is not because we are privileged to perform our judicial duty in that case and for reasons of convenience to disregard it in others. *The principle applies when rights either of persons or of property are protected by constitutional restrictions.* Under our system there is no warrant for the view that the judicial power of a competent court can be circumscribed by any legislative arrangement designed to give effect to administrative action going beyond the limits of constitutional authority." (Emphasis added.) This case and this statement were relied upon by us in the Drummey case (*supra*, 13 Cal.2d 75, 85) and no information has been presented to me to show that the rule there set forth has been in any way changed. No clearer case than this could possibly be found to illustrate the evils to be avoided. Old company stockholders and policyholders have been, and are, at the "mercy" of administrative officials; those officials may, during the last 10 years, have been either "expert and impartial" or "subservient."

I have heretofore set forth at length the self-evident fact that appellants are possessed of vested property rights of which they are being deprived. In *Ohio Valley Water Co.* v. *Ben Avon Borough*, 253 U.S. 287, 289 [40 S.Ct. 527, 64 L.Ed. 908], it was held: "The order here involved prescribed a complete schedule of maximum future rates and was legislative in character. *Prentis* v. *Atlantic Coast Line R. Co.*, 211 U.S. 210 [29 S.Ct. 67, 53 L.Ed. 150]; *Lake Erie & W. R. Co.* v. *State Public Utilities Com.*, 249 U.S. 422, 424 [39 S.Ct. 345, 63 L.Ed. 684]. In all such cases, *if the owner claims confiscation of his property will result, the state must provide a fair opportunity for submitting that issue to a judicial tribunal for determination upon its own independent judgment as to both law and facts: otherwise the order is void because in conflict with*

the due process clause, fourteenth amendment. Missouri Pac. Ry. Co. v. *Tucker,* 230 U.S. 340, 347 [33 S.Ct. 961, 57 L.Ed. 1507]; *Wadley Southern Ry. Co.* v. *Georgia,* 235 U.S. 651, 660, 661 [35 S.Ct. 214, 59 L.Ed. 405]; *Missouri* v. *Chicago, B. & Q. R. Co.,* 241 U.S. 533, 538 [36 S.Ct. 715, 60 L.Ed. 1148]; *Oklahoma Operating Co.* v. *Love,* 252 U.S. 331 [40 S.Ct. 338, 64 L.Ed. 596]." (Emphasis added.)

Appellants here complain bitterly because the mutualization plan provides that the price to be paid for new company's stock (of which they are the *beneficial owners*) is $3,000,000 while that same amount was originally taken out of old company's funds to purchase new company's stock and, *in addition,* all the other assets of old company (over $200,000,000 in assets plus such intangibles as going agency organization and concern, good will, etc., "worth several millions of dollars" [*Carpenter* v. *Pacific Mut. L. Ins. Co.,* 10 Cal.2d 307, 325 (74 P.2d 761)]) were turned over to new company! It surely must be crystal clear to everyone who can think that such an outrageous confiscation of property without due process of law has never before taken place in this state.

Evidence

In the trial court the evidence consisted of all of the record of the proceedings before the insurance commissioner, consisting of the reporter's daily transcript, the exhibits and the commissioner's decision. Appellants contend that they were prohibited from introducing evidence, or offering to do so, because of the rulings of the trial court; that no issues of fact were litigated; that the court ruled that it was not empowered to exercise its independent judgment on the evidence taken before the commissioner. Respondents state that appellants were given leave to serve and

file a motion and affidavits relative to the introduction of additional evidence and failed to do so. The memorandum opinion and order (July 2, 1951, Clk. Tr., 237-239) contains this statement: "After a careful study of the briefs submitted and the authorities cited I have come to the conclusion that, so far as any matter of fact is concerned, this Court is limited to determining whether or not the findings of the Commissioner are *supported by substantial evidence in the light of the whole record, but that it is for this court to exercise its independent judgment in interpreting the Rehabilitation Agreement and in construing and applying section 11527* of the Insurance Code. . . .

"I have come to the further conclusion that this Court cannot receive any additional evidence, but that upon proper showing may remand this matter to the Commissioner to take further evidence and reconsider the case in the light of such evidence. . . ."

Appellants point to the statements made by the trial judge on the settlement of findings that *"I think it must be very evident if I had had this case to decide on a new question of fact my decision might have been the opposite"* (emphasis added; page 766, Rep. Tr.) and "It [fixing the price] is very complex, and I think you are making it more complex. My finding was, and the basis of my determination was that they [the price determination committee] had a reasoned basis in fixing the price. That is the fact. If they had acted unreasonably then I would have had to set it aside. It was only because I could not convince myself that it was not a rational conclusion that they acted upon that I ever decided the case the way I did. *Because I could not take the facts and arrive at the same conclusion; not by a long shot. But because I did not feel that I could substitute my opinion for theirs, or substitute my opinion for the Commissioner's, that is the reason I arrived at the conclusion that I did.* But that is the crux of it. It is not the details that

they took in. What you are entitled to find now is entirely evidentiary." (Emphasis added.) The inference from this is obvious—that had the involuntary procedure been followed, the court would have withheld its approval because the plan did not protect the interests of those owning the beneficial interests.

The just-quoted statement made by the trial court shows, without equivocation, that had there been a trial de novo his decision would have been contrary to that reached. His statement shows that he was convinced that the weight of the evidence was with appellants but, believing himself limited by the substantial evidence rule, his conclusion was in favor of respondents. The only rational conclusion to be drawn from the facts of this case is that appellants were possessed of a vested property right and, therefore, should have been given a trial de novo in a *judicial tribunal* provided by the state for the protection of private property rights. Because appellants were not afforded a trial de novo they have been deprived of their property without the due process of law guaranteed to them by both the state and federal Constitutions.

Summary of Major Points

(1) It is my opinion that the provisions of the Insurance Code relating to voluntary mutualization of solvent insurance companies were not applicable to new company. As I have heretofore pointed out, new company was organized because of the insolvency of old company and cannot be considered as a solvent company until the liabilities arising from the non-can policies have been paid or sufficient funds accumulated to pay them. The voluntary mutualization provisions of the code in and of themselves show that they were intended by the Legislature to apply to not only a *solvent* company but to a company not so closely supervised

by the commissioner as the one here under consideration. The ordinary solvent company is not such a hybrid as we have in new company. In using the voluntary procedure, we have the commissioner, acting as conservator and beneficial owner of the stock of new company, agreeing to vote for the plan of mutualization as proposed by the price determination committee. As conservator, and beneficial owner of the stock of new company, he is *supposed* to be protecting the rights and interests of those in the position of appellants. When, as commissioner, he approves the proposed plan as fair and equitable, under the voluntary mutualization procedure, he is concerned with the fairness of the plan as it concerns those interested in new company. If the normal solvent company were being mutualized, the plan of mutualization would be proposed by the company itself, approved by its board of directors, adopted by a majority vote of its own shareholders, and then approved by the commissioner who, presumably, would not have seen the plan, or even heard of it, prior to the time it was presented to him for his approval as fair and equitable to those concerned—the shareholders and policyholders of the solvent company.

The following statement is found in the majority opinion: "In numerous cases where the action of an administrative officer was necessary *to prevent defeat of the statutory scheme*, his participation has been upheld although the grounds for disqualification were much more serious than those raised here." (Emphasis added.) The author again assumes too much. He assumes that the "statutory scheme" was being carried out. On the contrary, the statutory scheme is being *defeated*. The entire scheme for rehabilitation of insolvent corporations, and the statutory protection of the interested persons therein, is abrogated through the use of the procedure designed for mutualization of solvent corporations.

(2) I am also of the opinion that Paragraph 20(a) of the rehabilitation agreement has never before been judicially determined and, therefore, its provisions are not res judicata of the present controversy. I have pointed out that there is a separability clause in the rehabilitation agreement and that nothing heretofore done by this, or an appellate court, will be affected by a holding by this court that the parties may not validly contract to mutualize new company contrary to the applicable statutory provisions.

(3) There should have been a trial de novo in the superior court where evidence relative to the proper method to be used by the price determination committee, or *court-appointed* appraisers, could have been introduced by both sides and a determination made by a judicial trier of fact. Both appellants and respondents here devote many pages of their numerous briefs to such material. Such methods are obviously matters for experts in the field of insurance and should be the subject of testimony in the trial court.

(4) If, as I firmly believe, the procedure for involuntary mutualization of insolvent companies is the proper procedure, sections 1049, 1050, 1051 and 1052 of the Insurance Code contain detailed provisions for hearings and the appointment by the court of appraisers to appraise "the then outstanding shares of the capital stock of such insurer, without regard to any appreciation or depreciation arising out of said mutualization plan as so approved or modified. Such appraisement shall fix the reasonable value of such shares of capital stock, including the goodwill, if any, of such insurer, and shall state the value, if any, assigned to such goodwill; and if the appraisers shall have found that such insurer has no goodwill, such finding shall be stated. Such appraisement, when confirmed by said court, shall be final and conclusive." (§ 1051.)

The use of the involuntary mutualization procedure for an insolvent company follows logically from the original proceeding under sections 1010 and 1011. It should be noted that section 1054 (still under the Insolvency and Delinquency sections) provides that: *"Such insurer, after mutualization, shall be a continuation of the original insurer, and such mutualization shall not affect existing suits, rights or contracts except as provided in said mutualization plan as approved.* Such insurer, after mutualization, shall exercise all the rights and powers and perform all the duties conferred or imposed by law upon insurers writing the classes of insurance written by it, and to protect rights and contracts existing prior to mutualization, subject to the effect of said mutualization plan." (Emphasis added.)

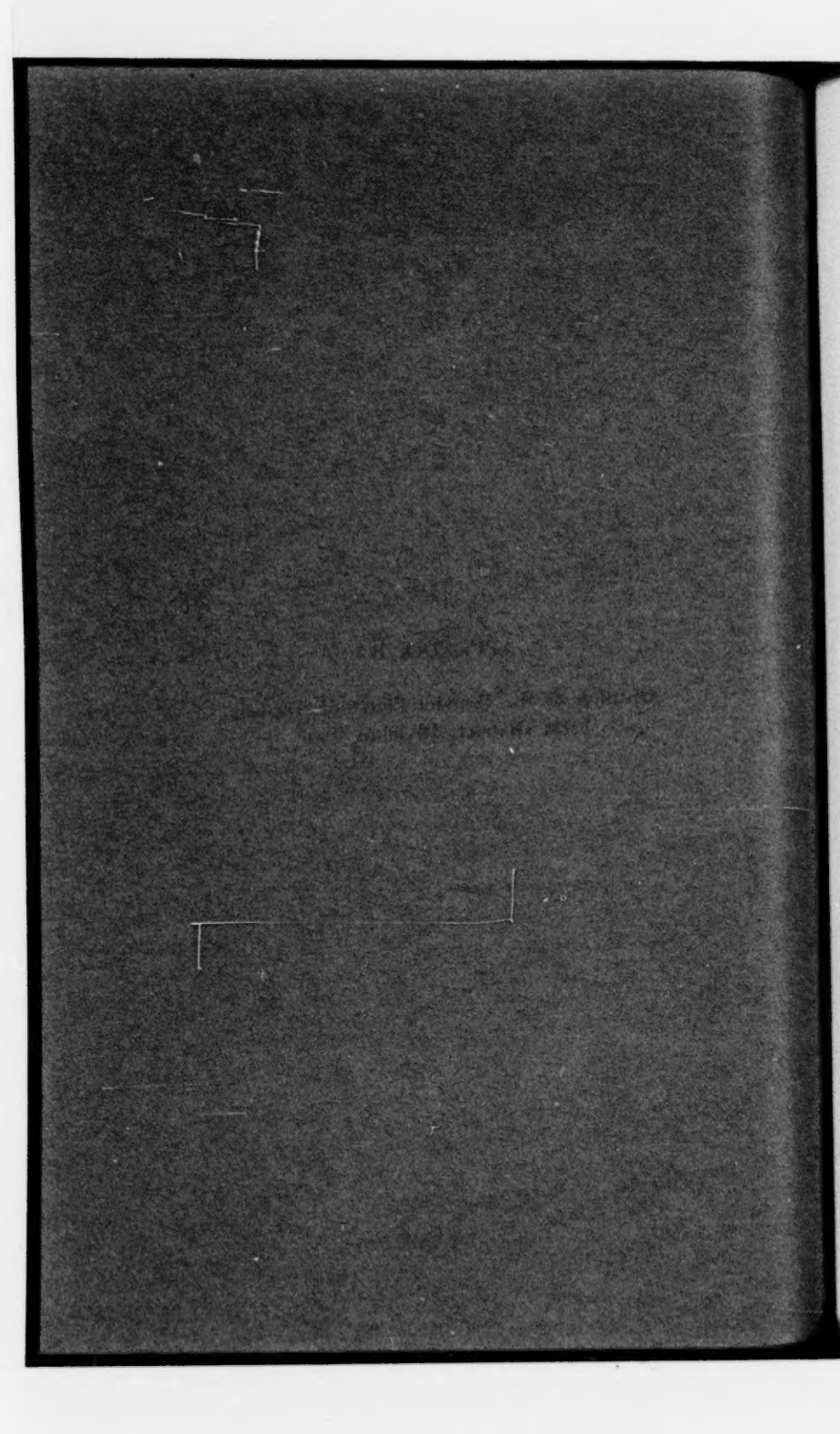
We held in *Carpenter* v. *Pacific Mut. L. Ins. Co.,* 10 Cal. 2d 307, 334 [74 P.2d 761], that "reinsurance" was a contract by which one company (new company) takes over the insurance risks of another company (old company) and becomes substituted as an insurer in the place and stead of the original insurer. This holding is also the logical result of following the procedure outlined in the Insolvency and Delinquency division of the Insurance Code.

From what Mr. Justice Traynor has said in his dissent and from the reasons heretofore set forth by me, the conclusion is *inescapable* that the judgment should be reversed.

SCHAUER, J.—I concur generally in the discussion, the reasoning and the conclusions of Mr. Justice Carter.

APPENDIX B

Opinion of the District Court of Appeal, First District, Division Two



APPENDIX B

Opinion of the District Court of Appeal, First District, Division Two

[Civ. No. 15977. First Dist., Div. Two. May 14, 1954, amended, June 11, 1954.]

The Pacific Mutual Life Insurance Company (a corporation) *et al.*, appellants, v. John R. Maloney, as Insurance Commissioner, etc., *et al.*, respondents.

Appeal from a judgment of the Superior Court of Los Angeles County. Paul Nourse, Judge. Affirmed.

Proceeding in mandamus to rescind order of Insurance Commissioner approving plan to mutualize an insurance company. Judgment denying writ affirmed.

Joseph L. Lewinson and Henry W. Low for appellants.

C. Ray Robinson and William B. Boone, as Amici Curiae on behalf of appellants.

O'Melveny & Myers, Paul Fussell, Homer I. Mitchell, James E. Cross, George B. Gose, Frank P. Doherty, Guy Knupp and Peery Price for respondents.

Lloyd W. Dinkelspiel and Heller, Ehrman, White & McAuliffe, as Amici Curiae on behalf of respondents.

GIBSON (Lilburn), *J. pro tem.**—This is an appeal from a judgment of the Superior Court, which denied a peremptory writ of mandate, and discharged an alternative writ previously issued.

The peremptory writ was sought under the provisions of Section 1094.5 of the Code of Civil Procedure to rescind an order of the Insurance Commissioner approving a plan to mutualize Pacific Mutual Life Insurance Company, a California corporation (referred to hereinafter as "New Company").

The alternative writ discharged by the judgment included an order staying the execution of the Plan of Mutualization. By stipulation a stay order was made by the

*Assigned by Chairman of Judicial Council.

District Court of Appeal, Second Appellate District, Division Three, prior to the expiration of the stay order made by the Superior Court. The stay order made by such appellate court is now in force.

The Plan of Mutualization was submitted to Honorable Wallace K. Downey as Insurance Commissioner in his character as an administrative officer, purportedly in pursuance to the provisions of subdivision (c) of Section 11526 of the Insurance Code (relating to the mutualization of nondelinquent stock companies), which provides that such a Plan of Mutualization must be approved by the board of directors of a company and its stockholders, and the Insurance Commissioner.

Order approving the plan was made after a hearing under Section 11527 of the Insurance Code, which provides:

"The commissioner shall examine the plans submitted to him under the provisions of subdivision (c) of Section 11526. He shall not approve such plan unless in his opinion the rights and interests of the insurer, its policyholders and shareholders are protected nor unless he is satisfied that the plan will be fair and equitable in its operation."

After the conclusion of the hearing Mr. Downey, as commissioner, made affirmative findings in accordance with the provisions of the section, and approved the Plan of Mutualization.

The petition for mandate alleges that the order of the insurance commissioner was made without jurisdiction and was not justified by the evidence.

Appellants, who were petitioners below (sometimes referred to herein as petitioners), are The Pacific Mutual Life Insurance Company of California, a California corporation (referred to hereinafter as "Old Company"), and Samuel K. Rindge, and others, who are stockholders in the Old Company, and the members of Pacific Mutual Shareholders Protective Committee.

In the receivership proceedings Honorable Samuel L. Carpenter, Jr., Insurance Commissioner of the State of California, first acted as conservator and then as liquidator of the Old Company, and several successors as Insurance Commissioners, including Honorable John R. Maloney, have acted as liquidator and Mr. Maloney now acts as liquidator.

Respondents below and here are the New Company and Mr. Maloney, as Insurance Commissioner of the State of California and as liquidator of the Old Company.

The order approving the Plan of Mutualization was made by Mr. Downey on September 22, 1950, at the time he was Insurance Commissioner of California and liquidator of the Old Company. He was named in the petition for mandate as a respondent, both in his character as Insurance Commissioner and as liquidator; but during the pendency of the proceeding in mandate, Mr. Downey was succeeded in both capacities by Mr. Maloney, and Mr. Maloney was accordingly substituted for Mr. Downey and the cause proceeded against Mr. Maloney in both capacities.

In 1936 The Pacific Mutual Life Insurance Company of California was in the possession of the Insurance Commissioner as conservator by reason of its insolvency. On December 4, 1936, by order of the court in the proceedings for the conservatorship of Old Company, title to all of the outstanding capital stock of New Company was vested in the Insurance Commissioner, as conservator of Old Company, subject to an option in favor of the participating life policyholders of New Company, giving them the right, after the expiration of approximately 10 years, to institute mutualization proceedings, that is, proceedings to cause New Company to purchase its capital stock for the purpose of converting the company from a stock company to a mutual company. Such option was contained in the rehabilitation and reinsurance agreement under the terms of

which the business of Old Company was rehabilitated by organizing a new and solvent company, which acquired most of the assets and assumed most of the liabilities of Old Company. The rehabilitation and reinsurance agreement is the source and basis of appellants' claim to the equitable interest in the proceeds of any sale of New Company stock that might be made by the Insurance Commissioner as liquidator (formerly conservator) of Old Company.

The rehabilitation and reinsurance agreement is also the source and basis of the right of the participating life policyholders of New Company to cause the company to acquire its stock (and thus accomplish its mutualization) at such price and upon such terms as might be fixed by a price determination committee, to be selected by the president of Stanford University, the provost of the University of California at Los Angeles, and the president of the Association of Life Insurance Presidents (the name of which was later changed to Life Insurance Association of America). That agreement, including the option in favor of the participating life policyholders of New Company, was, with the approval of Judge Henry M. Willis, after a hearing in the proceedings for the conservatorship of Old Company, executed by the conservator and by New Company. Judge Willis's order of approval, dated December 4, 1936, adjudged that the rehabilitation and reinsurance agreement was valid. Appeals were taken and the judgment was affirmed. (Carpenter v. Pacific Mut. Life Ins. Co., 10 Cal. 2d 307 [74 P. 2d 761]; Neblett v. Carpenter, 305 U. S. 297 [59 S. Ct. 170, 83 L. Ed. 182].)

In 1946, upon request of the requisite number of life policyholders, a price determination committee was appointed, and thereafter such committee determined that mutualization was practicable of accomplishment, promulgated a Plan of Mutualization, and fixed the price and

terms of payment at which the life policyholders of New Company should have the right to acquire the stock of New Company from the liquidator (who had by that time become successor of the conservator) of Old Company.

On September 22, 1950, the Insurance Commissioner, after a lengthy hearing, found that the Plan of Mutualization was fair and equitable to the stockholder, as well as to all other interested parties, and approved the plan.

In response to the petition for a writ of mandamus filed by appellants for the purpose of inquiring into the validity of the Insurance Commissioner's approval of the Plan of Mutualization there were presented to the Superior Court the questions of whether the Insurance Commissioner proceeded without or in excess of his jurisdiction, and whether the commissioner accorded a fair trial to those opposing the plan, and whether the commissioner committed any prejudicial abuse of discretion, particularly whether the commissioner proceeded in the manner required by law, and whether his approval of the plan was supported by substantial evidence in the light of the whole record. After a hearing, the judge of said court filed a carefully prepared opinion, in which he held that the Insurance Commissioner had not acted without or in excess of his jurisdiction, had accorded a fair trial to those opposing the plan, and had not abused his discretion in approving the plan.

Since appellants raise questions as to whether the rehabilitation and reinsurance agreement dated December 4, 1936, is valid in respect of the option to mutualize granted to the participating life policyholders; whether the validity of such agreement is *res judicata;* whether New Company, which has been carrying on a nationwide insurance business since 1936, should now be treated as insolvent for the purposes of mutualization; whether the requisite statutory steps were taken for mutualization of

New Company, and whether the price determination committee acted in good faith in fixing the price and terms of payment for the stock of New Company, it is essential to present in some detail what preceded the Insurance Commissioner's hearing as well as what took place at the hearing.

Old Company was engaged in the business of writing both participating and nonparticipating life insurance and accident and health insurance. The report of the regular Triennial Convention examination of Old Company made as of December 31, 1935, showed that Old Company was insolvent. The insolvency arose out of the fact that the premium rates charged by Old Company to the holders of noncancellable accident and health policies (hereinafter referred to as "non-can policies") were inadequate. The result was that the reserves for non-can policies were inadequate and Old Company was insolvent by at least $17,000,000. Said report was filed with the Insurance Commissioner on July 21, 1936. On July 22, 1936, pursuant to the provisions of Section 1011 of the Insurance Code, the Insurance Commissioner filed with the Superior Court in Los Angeles an application for an order appointing him conservator of Old Company and vesting in him title to all of the assets of that company. We shall hereafter refer to such proceedings as "conservatorship proceeding."

Said application was presented to Judge Douglas L. Edmonds, then presiding judge of said court, and Judge Edmonds on July 22, 1936, signed the order applied for. Pursuant to said order and pursuant to Section 1013 of the Insurance Code, which authorized seizure without notice or court order, the Insurance Commissioner took possession of all of the assets of Old Company. (Carpenter v. Pacific Mut. Life Ins. Co., *supra,* 10 Cal. 2d 307, 314-317).

On July 22, 1936, Judge Edmonds also signed "Order Permitting, Approving and Authorizing Rehabilitation Sale and Transfer of Assets and Reinsurance Plan and Agreement of The Pacific Mutual Life Insurance Company of California" pursuant to the provisions of Section 1043 of the Insurance Code. Said order, among other things, authorized the organization of New Company with a capital and surplus of $3,000,000, to be provided from the funds of the participating life division of the life department of Old Company. In addition thereto, the participating life division of the life department of Old Company was to furnish to New Company the sum of $1,792,-118.97 as a reserve for the non-can policies which were to be partially assumed by New Company under the rehabilitation agreement approved by Judge Edmonds. Said rehabilitation agreement further provided that the stock of New Company should be held by the Insurance Commissioner as conservator, subject to the right of New Company to become mutualized "as soon as legally possible."

In accordance with Judge Edmonds' order, the Insurance Commissioner organized New Company and the participating life policyholders contributed to New Company the total sum of $4,792,118.97, $3,000,000 of which constituted the capital and surplus of New Company, and $1,792,118.97 of which constituted a reserve for non-can policies which were to be partially assumed by New Company.

Said sum contributed by the participating life policyholders constituted all but $423,136.26 of the surplus of the participating life divisior of the life department of Old Company. Said sum had been earmarked for and was owned by the participating life policyholders of Old Company, because Old Company had conducted its participating life division as if it were a separate mutual life insurance company. A separate set of

books had been maintained for the participating life division; specific expenses had been charged to said division, separate surplus had been maintained for said division; separate annual statements had been prepared for said division, and the so-called "dividends" or returns of premium made to participating life policyholders had been charged against the funds of said division.

After the organization of New Company the commissioner, as conservator, in accordance with Judge Edmonds' order, transferred to New Company substantially all of the assets of Old Company. As consideration for such assets, New Company delivered to the conservator all of the capital stock of New Company, which he was to hold, subject to the provisions of the rehabilitation agreement approved by Judge Edmonds. On July 23, 1936, New Company intervened and became a party to the conservatorship proceeding. Shortly thereafter it was found that Justice Edmonds was the owner of a policy of life insurance issued by Old Company, and that he was, therefore, disqualified. It was ultimately held that his orders were void (Carpenter v. Pacific Mut. Life Ins. Co., *supra*, 10 Cal. 2d 307, 323).

Upon discovery of Judge Edmonds' disqualification, the application of the Insurance Commissioner for appointment as conservator of Old Company was assigned to and heard by Judge Henry M. Willis, and on August 11, 1936, Judge Willis made a new order appointing the Insurance Commissioner as conservator and ratifying an appointment theretofore made by Judge Edmonds. It was held that notwithstanding the invalidity of Judge Edmonds' orders, the conservator's seizure of the assets of Old Company was lawful (Carpenter v. Pacific Mut. Life Ins. Co., *supra*, 10 Cal. 2d 324). However, Judge Willis did not, on August 11, 1936, make any order with respect to the rehabilitation agreement theretofore approved by Judge Edmonds or with respect to the transfer of Old Company's assets to New

Company and the issuance of New Company's stock to the conservator. Nevertheless, New Company held the assets of Old Company and the conservator held all of the capital stock of New Company. In view of the fact that the rehabilitation of the business of an insolvent insurer and the transfer of assets of such an insurer can be made only with court approval (Ins. Code §§ 1043 and 1037 subd. d), the invalidity of Judge Edmonds' orders left the permanent status of the assets and the stock in suspense until Judge Willis's order of December 4, 1936, which will hereinafter be referred to.

During the period between July 22, 1936, and December 4, 1936, New Company acted as a corporate agent of the Insurance Commissioner to assist him in carrying on the business of the Old Company.

As was stated by the Supreme Court in the Carpenter case, *supra*: It was obvious that if the agency organization were to be preserved pending court approval of the rehabilitation plan, the business of the Old Company had to be continued. Faced with these facts, the commissioner determined to organize a New Company to continue the business pending the approval of a rehabilitation plan. And it was pending the approval of a rehabilitation plan that New Company acted as a corporate agent of the Insurance Commissioner. (Carpenter v. Pacific Mut. Life Ins. Co., *supra*, 10 Cal. 2d 307, 325.)

On August 29, 1936, Judge Willis ordered all interested parties to show cause why they should not approve the rehabilitation agreement which Judge Edmonds had theretofore purported to approve. Numerous parties, including individual stockholders and the Pacific Mutual Stockholders Protective Committee, filed objections to such rehabilitation agreement. (Carpenter v. Pacific Mut. Life Ins. Co., *supra*, 10 Cal. 2d 319.)

On September 25, 1936, the Insurance Commissioner filed a "Petition for Approval of the Rehabilitation and Reinsurance Agreement," attached to which was the rehabilitation and reinsurance agreement which constitutes the basis of the rights of the conservator and his successors as owners of all of the stock of the company, and the basis of the rights of appellants herein, who claim an equitable interest in the stock of New Company, and the basis of the rights of the participating life policy holders under the option contained therein to cause New Company to be mutualized. Said petition prayed for an order ratifying, confirming and approving the acts of the commissioner as conservator and causing to be formed, forming and subscribing to and purchasing the capital stock of New Company, and ratifying, confirming and approving the transfer and conveyance therefore made of the assets of Old Company to New Company. Said petition further prayed that the rehabilitation and reinsurance agreement be approved and that the conservator be authorized and directed to execute said agreement and to carry out its provisions.

On the same date, the court issued an order requiring Old Company, New Company, and all persons interested or claiming to be interested, either as policyholders or stockholders of Old Company, or otherwise, to show cause why the court should not make orders in accordance with the conservator's petition.

After a protracted hearing pursuant to said order to show cause, in which Pacific Mutual Stockholders Protective Committee, numerous individual stockholders and others were heard, Judge Willis made his order of December 4, 1936, in which he ratified, confirmed and approved the acts of the conservator in organizing and subscribing to and acquiring the capital stock of New Company, and in transferring to New Company the sum of $3,000,000

out of the assets in his hands as a conservator, and ratifying, confirming and approving the transfer and conveyance theretofore made of the assets of Old Company to New Company.

Said order approved "each and all of the terms and conditions" of the rehabilitation and reinsurance agreement and authorized and directed the conservator to enter into said agreement, and authorized him "without further order of this court, fully and faithfully to perform, carry out, and discharge each and all of the obligations, terms, conditions, and covenants on his part required to be performed under the terms of said Rehabilitation and Reinsurance Agreement," and "forever barred and enjoined [all persons] from making hereafter any complaint in respect of the said Rehabilitation and Reinsurance Agreement, or any provision or provisions thereof, except as in said agreement specifically permitted or by appeal from this Order; the prosecution by any person, firm, or corporation of any proceeding or proceedings of whatever kind or nature, for the purpose of attacking this Order, or any conveyance or transfer made pursuant hereto, (other than as permitted by said Rehabilitation and Reinsurance Agreement or by appeal from this Order)."

The Rehabilitation and Reinsurance Agreement provided for the transfer to New Company of substantially all of the assets of Old Company and for the reinsurance and assumption by New Company, at the election of the respective policyholders, of all policies of insurance other than non-can policies, and on reduced rates of benefit, for reinsurance and assumption by New Company at the election of the policyholders of all non-can policies of insurance. It provided that New Company should establish a participating department, whose assets should be held and whose business should be carried on in the same manner as if it constituted a separate mutual life insurance company.

It further provided that New Company should establish a separate department for its Nonparticipating Life Insurance, and a separate department for its Accident and Health Insurance, and that any surplus existing in said departments might be used for general corporate purposes subject to limitations contained in Paragraph 14 of said agreement.

In Paragraph 14 it was provided that a special fund should be established from funds available for general corporate purposes for the purpose of completely restoring the non-can benefits which had been reinsured and assumed on reduced basis. It was further provided that there should be transferred to such fund such amounts as the board of directors should in its discretion determine to be not reasonably required for the reasonable, proper and profitable conduct of the operations of New Company as a going concern. It was further provided that at the time of any examination of New Company by the Insurance Commissioner, the commissioner might require the transfer of additional funds to such special fund, to the extent that such additional funds available for general corporate purposes were, in his opinion, available without interfering with the proper and profitable conduct of the business of New Company as a going concern.

These provisions with respect to restoration of non-can benefits were made "to the end that the benefits originally provided in said Non-Can Policies as written may eventually be fully paid, including eventual full payment of benefits becoming due prior to the time of such restoration, with interest on deferred restoration payments of such benefits at the rate of three and one-half percent (3½%) per annum."

The Rehabilitation Agreement provided for the transfer to New Company from the participating division of the life department of Old Company of the sum of $3,000,000 as

capital and surplus and of the sum of $1,792,118.97 as a reserve for the Accident and Health Department, and further provided for the transfer to New Company, for its general corporate purposes, of not to exceed 10 per cent of the net profits on participating policies reinsured pursuant to said agreement. Profits from participating policies thereafter written were not to be affected thereby and were to be held in the walled-off participating department of New Company.

Paragraph 20(a) of the Rehabilitation and Reinsurance Agreement created an *option* in favor of the participating life policyholders to cause the company to be mutualized under the conditions specified therein. Said right of the participating life policyholders was referred to in Paragraph 20 as "an option to mutualize." It was provided therein that after a period of approximately 10 years, 10 per cent of the participating life policyholders could request the creation of an appointing committee to exercise duties in respect of a mutualization of New Company for the benefits of the departments of New Company designated by such policyholders; that the appointing committee should designate a price determination committee; that the price determination committee should determine whether, in its opinion, mutualization of New Company was then practicable and that, if it determined that mutualization was then practicable it should determine the proper price to be paid for the stock of New Company upon such mutualization and appropriate terms of payment. Said agreement provided further, in order that said option might be an effective option, binding upon the stockholder of New Company and all others claiming through such stockholder, that the conservator, as sole stockholder, for himself and for any successors in ownership of said stock, agreed to consent and consented to such Plan of Mutualization as might be promulgated by the price determination

committee and to dispose of such stock at the price and upon the terms of payment provided for in such Plan of Mutualization.

Various provisions of the Rehabilitation and Reinsurance Agreement show that the agreement contemplated that the price determination committee could promulgate a Plan of Mutualization and fix the price and terms of payment for the stock prior to the full restoration of non-can benefits; and that in such case payment for the stock would be postponed until after restoration of non-can benefits had been completed. Inherent in the fact that the agreement contemplated such postponement of payment, is a further fact that the agreement contemplated that the Plan of Mutualization should not obligate New Company unconditionally to make the postponed payment.

Appeals were taken from Judge Willis's order of December 4, 1936, adjudicating the validity of the Rehabilitation and Reinsurance Agreement and the Supreme Court of California and the Supreme Court of the United States affirmed the order. (Carpenter v. Pacific Mut. Life Ins. Co., *supra.*)

The result of Judge Willis's order of December 4, 1936, was that New Company acquired valid title to substantially all of the assets of Old Company and the conservator acquired valid title to all of the capital stock of New Company, subject, however, to an option to the participating life policyholders of New Company, through mutualization proceedings initiated after approximately 10 years, to cause New Company to acquire such stock at the price and upon the terms fixed by a duly appointed price determination committee, in the event that such committee should determine that in its opinion mutualization was practicable. The option required that the mutualization proceedings should be conducted in accordance with the laws of the State of California.

On February 2, 1937, the court, in the conservatorship proceedings, ordered the liquidation of Old Company and appointed the Insurance Commissioner to liquidate it. The validity of this order was upheld on appeal. (Carpenter v. Pacific Mut. Life Ins. Co., 13 Cal. 2d 306 [89 P. 2d 637].)

Thus, the liquidator succeeded the conservator, as the owner of the stock of New Company, subject to the option in favor of the participating policyholders to cause the company to be mutualized.

On April 4, 1938, the liquidator transferred title to the capital stock of the New Company to voting trustees. This was done pursuant to the provisions of section 1037(e) of the Insurance Code. The validity of this transfer under the voting trust was upheld upon appeal. (Caminetti v. Pacific Mutual L. Ins. Co., 22 Cal. 2d 344 [139 P. 2d 908].)

Under the provisions of the voting trust, the trustees were given full legal title to the stock in order that they might exercise the rights of stockholders in the control of the corporation, and they were expressly obligated to carry out all of the provisions of the Rehabilitation and Reinsurance Agreement, including the covenant of the conservator, for himself and his successors in the ownership of the stock, to consent to any Plan of Mutualization promulgated by a duly appointed price determination committee.

Thus, the voting trustees held the stock of New Company subject to the option to mutualize contained in the Rehabilitation and Reinsurance Agreement. The voting trust provided that it should terminate upon adoption of a Plan of Mutualization in accordance with the laws of the State of California.

In 1946, approximately 10 years after the organization of New Company, the requisite percentage of participating

life policyholders requested the creation of an appointing committee to exercise the duties and functions provided for in the Rehabilitation and Reinsurance Agreement in respect of a proposed mutualization of New Company. The participating life policyholders, as permitted by the agreement, specified that the mutualization should be for the benefit of both participating and non-participating life policyholders. As of January 31, 1947, in accordance with the terms of said agreement, George Willard Smith, President of the Life Insurance Association of America (formerly the Association of Life Insurance Presidents), Doctor Donald B. Tresidder, President of Stanford University, and Doctor Clarence A. Dykstra, Provost of the University of California at Los Angeles, appointed a price determination committee consisting of Alva J. McAndless, Ray D. Murphy, Horace R. Bassford, and Albert J. Hettinger. Mr. McAndless was the President of Lincoln National Life Insurance Company of Fort Wayne, Indiana, a stock company, and the tenth largest life insurance company in the United States. He was a graduate of the University of Michigan and an actuary by profession. He was a past president of the American Institute of Actuaries (now called the Society of Actuaries) and a past president of the American Life Convention. He had been connected with Lincoln National Life Insurance Company since 1919 and had risen through the ranks, holding various positions and offices until he became president in 1939. He had had extensive experience in evaluating other life insurance companies through the acquisition of stock companies, either by way of acquiring their stock or their assets. Among the acquisitions with which he was familiar or in which he personally participated were acquisitions which Lincoln National Life Insurance Company made of Michigan State Life Insurance Company, Pioneer Life

Insurance Company, Merchants Life Insurance Company, Globe Life Insurance, American Life Insurance Company, Reinsurance Life Insurance Company, Old Line Life Insurance Company, Northern States Life Insurance Company, and Royal Union Life Insurance Company. In addition thereto, he had handled negotiations for the purchase of Illinois Life Insurance Company and Missouri State Life Insurance Company, but in those instances Lincoln National Life Insurance Company did not become the purchaser.

Mr. Murphy was the Vice President and Chief Actuary of the Equitable Life Assurance Society of the United States, one of the five largest life insurance companies in the country. He is a graduate of Harvard University and an actuary by profession. He had been with Equitable Life since 1913. He was a past president of the Actuarial Society of America. Since 1936 he had been responsible at Equitable Life for all valuations of life and accident and health contingencies, including noncancellable accident and health contracts. He was responsible at Equitable Life for mortality and morbidity investigations and for analysis of all sources of profits and losses, and for distribution of surplus based upon such analyses. His duty caused him to be involved in many studies and estimates of projected future profits and losses and the effect of future contingencies upon the operations of Equitable Life.

Mr. Bassford was Vice President and Chief Actuary of Metropolitan Life Insurance Company, the largest life insurance company in the United States. He was a graduate of Trinity College and had been associated with Metropolitan Life since 1915. He was a Vice President of the Actuarial Society of America. He had participated in the acquisition by Metropolitan Life of several life insurance companies, including Pittsburg Life and Trust Company, Niagara Life Insurance Company, and Golden Seal Asso-

ciation, in connection with which it was necessary for him to evaluate said companies.

Mr. Hettinger was a partner in the investment banking firm of Lazard Freres and Company. He was a graduate of Stanford University and received the degree of Doctor of Philosophy in Business Economics at Harvard University, where he served for a number of years as Professor of Business Economics in the Harvard Graduate School of Business Administration. As a member of the Harvard faculty he had supervised research work in the valuation of life insurance stocks, and during the same period acted as economist to the Governor of the Federal Reserve Bank of Boston. He became engaged in business in the investment field in 1926 and became a partner in Lazard Freres and Company in 1943. During his business life he had made a particular study of life insurance stocks and their values.

Following their appointment on January 31, 1947, the members of the price determination committee undertook to perform the duties and responsibilities entrusted to them. They employed as their actuary Joseph A. Christman, Associate Actuary of the Metropolitan Life Insurance Company of New York. He was a Fellow of the Actuarial Society of America and had served in the Actuarial Division of Metropolitan Life since 1926. In the performance of his duties for Metropolitan Life, approximately 600 employes worked under his supervision. Associated with him in the duties which he performed for the price determination committee were D. J. van Keuren and F. H. Byron, both employes of the Metropolitan Life and Fellows of the Actuarial Society of America. Mr. Christman and his colleagues had the assistance of numerous trained supervisory and clerical employes borrowed from Metropolitan Life and Equitable Life.

Commencing in 1947, the members of the price determination committee, with the assistance of Mr. Christman

and his associates, undertook a study of the past and anticipated future earnings of New Company, of the amount which would be required completely to restore non-can benefits, of the length of time which would be required to accomplish such restoration, and of the value of the stock of that company. Their study occupied a period of approximately three years and consumed approximately 10,000 hours of work. Mr. McAndless testified that the committee made "one of the most complete investigations of earning power that has ever been made for any life insurance company."

On April 4, 1950, the price determination committee rendered its report, stating that in its opinion mutualization of New Company was then practicable, determined the value of the stock as of December 31, 1948, and fixed the price to be paid for the stock of New Company at $3,000,000 plus interest on $3,000,000, from December 31, 1948, to date of payment, with certain provisions for its augmentation, and fixed the terms of payment.

The Plan of Mutualization provides for a special surplus fund, to be accumulated from 5 per cent of the net profits of the participating department on policies issued subsequent to July 22, 1936, and for a payment of the purchase price from this fund and from capital in general corporate surplus. The Plan of Mutualization filed by the committee as part of its report, provided that upon adoption of the plan, the Voting Trust Agreement of April 4, 1938, should terminate in accordance with the provisions of said voting trust and that the liquidator to whom the voting trustees were obligated to transfer the stock should immediately dispose of the stock of New Company by transferring it to trustees under a new voting trust, in accordance with the provisions of Insurance Code, Section 11529.5. It was expressly provided that nothing contained in the plan should affect the right of the

non-can policyholders to have applied to restoration of non-can benefits all of the corporate earnings of the company not reasonably required for the reasonable, proper and profitable conduct of the operations of New Company as a going concern, as provided in Paragraph 14 of the Rehabilitation and Reinsurance Agreement.

The plan further provided that in accordance with such agreement New Company should submit the plan to the policyholders entitled to vote thereon and that if 10 per cent of such policyholders should so request New Company should submit the plan for approval in accordance with the laws of the State of California.

The plan was submitted to the life policyholders and the requisite percentage requested its submission for approval in accordance with the laws of the State of California. In accordance with Section 11526 of the Insurance Code, New Company submitted the plan for the required approvals; on May 5, 1950, the board of directors of New Company adopted the Plan of Mutualization. Thereafter, a majority of the voting trustees under the Voting Trust Agreement of April 4, 1938, as owners and holders of the stock of New Company, and in accordance with the provisions of said Voting Trust Agreement, approved the Plan of Mutualization by executing their written consent thereto. Under the provisions of the Voting Trust Agreement the action of a majority of the trustees constituted action of all of the trustees.

On or about June 16, 1950, New Company submitted the Plan of Mutualization to the Insurance Commissioner and petitioned for the approval thereof. The Insurance Commissioner gave notice by publication and by mail that a hearing would be held on August 1, 1950, for the purpose of determining whether the Insurance Commissioner should approve the plan. Notice of the hearing was mailed, among others, to Old Company and to the

Pacific Mutual Stockholders Protective Committee. On August 1, 1950, the hearing commenced, and continued from day to day until and including August 18, 1950. All persons desiring to be heard were heard, including the Pacific Mutual Stockholders Protective Committee. Old Company did not avail itself of the opportunity to be heard. Evidence both oral and documentary was received, and was incorporated in a reporter's transcript of over 500 pages.

On September 22, 1950, the Insurance Commissioner issued a 22-page decision, in which he found that the Plan of Mutualization protected the rights and interests of New Company, its policyholders and its shareholders, and that the plan would be fair and equitable in its operation, and in which he issued his approval, thus permitting the plan to become effective if it should be approved by a majority vote of the life policyholders and should thereafter be filed in the office of the Insurance Commissioner. (Ins. Code, §11526.)

The life policyholders of New Company thereafter approved the Plan of Mutualization in accordance with Section 11526(d) of said Code.

On or about November 9, 1950, before the plan was filed in the office of the Insurance Commissioner, after having been adopted by a vote of the directors of New Company, and after having been approved by the written consent of the shareholders of New Company and by the Insurance Commissioner (but before its approval by the life policyholders of New Company) appellants filed their petition for writ of mandamus and obtained an order staying the operation of the Insurance Commissioner's approval of September 22, 1950, expressly permitting, however, a vote of the life policyholders in accordance with Section 11526(d) of the Insurance Code.

In accordance with the provisions of the Code of Civil Procedure, Section 1094.5, a hearing was held by the court below. All of the record of the proceedings before the Insurance Commissioner was filed with the court. Appellants, respondent Insurance Commissioner, and respondent New Company each filed lengthy briefs and lengthy arguments were made, which are reported in the Reporter's Transcript on Appeal. No evidence was received other than stipulations and the record before the Insurance Commissioner, consisting of the Reporter's Daily Transcript, the exhibits and the Insurance Commissioner's decision. On March 24, 1952, the judge of the court filed his memorandum of decision, and on June 2, 1952, he filed his findings of fact, conclusions of law and judgment, which are the subject matter of the appeal herein.

We will now proceed to a consideration of the law of the case. As above indicated, the principal points raised by appellants are two:

(1) The order made by the Insurance Commissioner was not justified by the evidence; and

(2) The order was made without jurisdiction.

We think neither claim is tenable and that the judgment of the lower court must be affirmed.

Point (1) may be rather quickly disposed of. After notice to all interested parties, a hearing, which took 13 days to complete, was had by the commissioner. Much evidence, both oral and documentary, was received by him. It is manifestly impossible to here set it forth at length. Suffice it to say we have examined it in detail, all of the volumes of the daily transcript of the evidence and the exhibits introduced, and we are not prepared to say that such evidence then taken and received was insufficient to justify the commissioner's ultimate conclusion that the

plan was fair and equitable to, and protected the rights and interests of, all interested parties, including the stockholder, in whose right the appellants sue.

On the contrary, much of the evidence was based upon thousands of hours of study and investigation by persons who appear to have been well qualified experts, and we are well satisfied the commissioner acted upon adequate evidence. Two members of the Price Determination Committee and one of the actuaries employed by the Price Determination Committee testified at length as to the manner in which, and the basis upon which, the committee arrived at the price to be paid by New Company for its stock when it consummated the proposed Plan of Mutualization. In substance they testified that they had, by long and exhaustive actuarial studies, determined the amount necessary to fully but gradually restore the benefits of the non-can policyholders; that they had then discounted these amounts at 3 per cent interest to their present value, and found that the present value of the amounts necessary for restoration was $22,000,000; that by similar studies they had established the probable earnings of New Company for each year, commencing with the year 1949 and extending to the year 2000; that by discounting the earnings for the years 1949 to 1974, both inclusive, at 3 per cent (only a portion of the earnings for the last year were so discounted), they determined that the company would be able to complete restoration of non-can benefits in the year 1974; that after the completion of restoration the stockholders of Old Company would be entitled to its earnings, and that the present value of these earnings from 1974 to perpetuity, discounted at 10 per cent, was $2,614,000; that by reason of the terms of the rehabilitation agreement it was necessary to add $500,000 to this amount, but that if certain risk elements had been disregarded, they thought it proper to deduct

the sum of approximately $100,000, giving a present value to the stock of $3,000,000; that the calculated earnings upon which their estimate of the time within which to complete restoration of non-can benefits could be made, and upon which they base the present value of future earnings, were net earnings, after provision for contingency reserves.

They also testified that in their opinion a buyer could be found who would be willing to presently pay $3,000,000 for the stock of New Company and await the right to participate in the earnings of New Company for 25 years; that the stock of large life insurance companies currently had sold at 4.3 to 7.8 times of their estimated earnings after the deduction of voluntary reserves; that if the estimated earnings of New Company from 1948 to perpetuity were discounted to their present value at 10 per cent, that value would be less than the amounts necessary for full restoration, and there would be nothing left for the stockholders; that if the present value of the stock were fixed by giving a value to the nonparticipating life insurance in force at $20 per thousand, the value of the stock would be less than the amount necessary for restoration, and that, in their considered opinion, the price of $3,000,000 was a fair one to be paid to the stockholders.

They also testified that because the payment of the present value of the stock as determined by them was not to be made immediately, but was to be deferred, they had provided for the payment of interest upon the $3,000,000 and instead of fixing a rate of interest had used the basis of the highest coupon rate paid on long term government bonds, as they thought that would be equal to the amount New Company could earn upon the deferred payment from year to year; that they recognized that if restoration was completed sooner than they estimated, that is, prior to 1974, this would give an added value to the

stock and that they believed $250,000 for each year by which the date of restoration preceded 1974, was a fair estimate of the increased value.

There was introduced into evidence the report of the actuaries who had made the studies upon which the cost of restoration of future earnings were based, and in which the method and the data used are set forth in detail; and much other direct and pertinent evidence.

Some point is made of the fact that some evidence available was not spread upon the record. In view of the foregoing, such is of no consequence. And, in any event, there is nothing in Section 1094.5, Code of Civil Procedure, or any other law we know of in proceedings such as this, which requires the spreading of detailed facts upon the record. (Popcorn Equipment Co. v. Page, 92 Cal. App. 2d 448, 451 [207 P. 2d 647]; *In re* Atlas Pipeline Corp., 39 F. Supp. 846, 848.) All that is required is that the commissioner's approval be supported by substantial evidence in the light of the whole record, and if such be the case, as we now hold it was, the court below and this court are bound thereby. (Thompson v. City of Long Beach, 41 Cal. 2d 235, 239-240 [259 P. 2d 649]; Rible v. Hughes, 24 Cal. 2d 437, 445 [150 P. 2d 455, 154 A. L. R. 137]; Housman v. Board of Medical Examiners, 84 Cal. App. 2d 308, 315 [190 P. 2d 653]; Republic Aviation Corp. v. National Labor Relations Board, 324 U. S. 793, 800 [65 S. Ct. 982, 89 L. Ed. 1372, 1377, 157 A. L. R. 1081].)

Point (2). We shall now proceed to a consideration of the question of jurisdiction and related matters. We think it proper to first consider the issue of *res judicata*. In this respect the appellants contend that the order of December 4, 1936, approving the Rehabilitation and Reinsurance Agreement is not *res judicata* as to such agreement, nor is it *res judicata* as to the Plan of Mutualization.

As to the first contention, we are foreclosed from considering it for the Supreme Court has already decided the point contrary to appellants' claim. In Carpenter v. Pacific Mut. Life Ins. Co., 13 Cal. 2d 306, 309 [89 P. 2d 637], the court said: "The legality of the seizure and the lawfulness and propriety of the plan of rehabilitation have already been upheld by this court. (Carpenter v. Pacific Mut. Life Ins. Co., 10 Cal. 2d 307 . . . affirmed with opinion, Neblett v. Carpenter, 305 U. S. 297 [. . . . 83 L. Ed. 182].)"

The California courts have quite uniformly held that when the validity of an agreement is adjudged in a prior proceeding, that issue is *res judicata,* even though a litigant in a later proceeding may urge some reason for its alleged invalidity which was not urged in the prior proceeding. (Price v. Sixth District Agricultural Assn., 201 Cal. 502, 509 [258 P. 387]; De Hart v. Allen, 26 Cal. 2d 829, 831 [161 P. 2d 453].)

In proceedings in which attacks have been made upon the validity of similar plans of rehabilitation after an adjudication of the validity of such plans, the courts have held the issue of validity to be *res judicata* as to all parties represented in the proceedings for the approval of such rehabilitation plan, as to persons in privity with such parties, and as to parties represented by them through class representation. (Thrower v. Kistler, 14 F. Supp. 217, 219, 221; National Surety Corp. v. Nantz, 262 Ky. 413 [90 S. W. 2d 385, 388].)

The fact that a series of orders were contemplated does not change the rule. One of a series of orders in a proceeding becomes *res judicata* if the order is appealable and not appealed from or if an appeal is taken and is affirmed on appeal. (Estate of Nolan, 145 Cal. 559, 561 [79 P. 428]; Baldwin v. Stewart, 218 Cal. 364, 367-368 [23 P.2d 283].)

The issue of the Rehabilitation and Reinsurance Agreement was fully litigated in an adversary proceeding, and not by default. We have examined the authorities cited by appellants in support of their contention in this regard and find that they are not, in our opinion, authority for that which we are now investigating.

Appellants urge that before approving the Plan of Mutualization as fair and equitable the Insurance Commissioner was in duty bound to determine the value of the New Company as a going concern by ascertaining its earning capacity and capitalizing the same at an appropriate rate on the basis of economic surveys and special studies of the relevant criteria. In this case it was not necessary, as a matter of law, to employ any one method of determining the value of the stock. Such stock could be evaluated either on the basis of the market value, capitalization (so-called going concern and investment value), or on the basis of the usual method of evaluating all the stock of an insurance company. (California Annual Conf. of M. E. Church v. Seitz, 74 Cal. 287, 296 [15 P. 839]; Rives-Strong Bldg., Inc. v. Bank of America, 50 Cal. App. 2d 810, 816 [123 P. 2d 942]; Bewick v. Mecham, 26 Cal. 2d 92, 94-98 [156 P. 2d 757, 157 A. L. R. 1277].) At any rate, the Price Determination Committee did determine the investment value (or going concern value) of the stock, on the basis of a capitalization of corporate earnings applicable to the stockholders' equity.

In estimating future earnings there appears to be no specific criteria to go by. As the United States Supreme Court has said: "The extent and method of inquiry necessary for a valuation based on earning capacity are necessarily dependent on the facts of each case." (Consolidated Rock Products Co. v. Du Bois, 312 U. S. 510, 527 [61 S. Ct. 675, 85 L. Ed. 982, 994].) The pattern

of future earnings of the New Company having been fixed by the committee, upon sufficient evidence, we can see no objection to the plan adopted for capitalization. (Akron, Canton & Youngstown Ry. Co. v. Hagenbuch, 128 F. 2d 932, 939.)

The next point urged is that the Insurance Commissioner made no pretense of determining investment value in the manner required by law or otherwise; his order approving a Plan of Mutualization, therefore, was due to a mistake of law and must be reversed as arbitrary and constructively fraudulent. One answer to this is that the power and duty to determine the value and price of the stock was lodged in the Price Determination Committee and not in the Insurance Commissioner, by the Rehabilitation and Reinsurance Agreement, and this committee was thereby empowered to determine the price to be paid for the stock on any reasonable basis. The determination of value was made by the committee after considering several conventional and approved methods, and we are unable to hold, from the record, that the conclusion it arrived at was unreasonable.

Appellants complain that $3,000,000 was arbitrarily taken away from the stockholders by adding $3,000,000 to the estimated cost of restoration. We find this item to be fully explained in the Christman Report and in his testimony and we can find nothing arbitrary in his calculations. It is based on detailed study by actuaries.

In answer to appellants' contention to the contrary, we find it could well have been found, upon the evidence, that the Mutualization Plan did adequately protect the rights and interests of shareholders.

Appellants next contend that by approving Paragraph 20(f) of the Rehabilitation and Reinsurance Agreement, the court thereby reserved the jurisdiction to determine, at a future time, whether the provisions as to mutualization

in Paragraph 20 were contrary to law or illegal or void. We can see no merit in the contention. If the court had intended to reserve such power it would have said so. There is nothing in the order to that effect, and we should not and cannot read something into it that is not there. It is further urged that Paragraph 16 of Judge Willis's order of December 4, 1936, shows that the order is not *res judicata* as to the Rehabilitation and Reinsurance Agreement. The fact that the court therein reserved jurisdiction to make further orders in the premises, does not stultify, or set at naught, the order already made. This paragraph was obviously intended to permit the court to thereafter make whatever order it deemed proper, if any, to carry the order then being made along to fruition. (Cason v. Glass Bottle Blowers Assn., 37 Cal. 2d 134 [231 P. 2d 6].)

Passing now to the next contention of appellants, that the order of December 4, 1936, is not *res judicata* as to the Mutualization Plan proposed, we must, of course, agree, since the court could not then approve a plan which was not before it, nor, indeed, had it then been formulated; but what it did do was to approve the agreement in all of its details, and one of those details was to give the participating life policyholders the *right or option* to mutualize thereafter. The decreeing of this *right* is, therefore, *res judicata*. We are satisfied that the order we have been discussing has become *res judicata* as to all the matters determined therein.

We now pass to another point urged by appellants, and that is that sections 1043-1052 of the Insurance Code, and not sections 11526-11533, are applicable to the mutualization of the New Company.

In the first place, the rehabilitation agreement above referred to unquestionably makes sections 11525, etc., applicable to the mutualization of the New Company, and this agreement has been approved by the court, thus becoming

res judicata. In the second place, these sections (11526-11533) would have been applicable in any event, because the New Company is a solvent insurer and not one that has been seized by the commissioner. Paragraph 20(a) of the agreement approved by the court, provides machinery for the formation of a "voluntary mutualization of the New Company, in accordance with the laws of the State of California." Under such law a voluntary mutualization can be accomplished only under the provisions of section 11525, etc., of the Insurance Code and not under the provisions of section 1043, etc., thereof. This being the case, it would seem unnecessary to consider the other points raised by counsel in this regard, since to do so would merely be reconsidering something that has already been decided by the Supreme Court.

The contention is made that the court must disregard the corporate entity of the New Company and treat it as though it were the Old Company. This matter has already been decided contrary to such claim. (Garrison v. Pacific Mut. Life Ins. Co., 83 Cal. App. 2d 1, 9 [187 P. 2d 893].)

There is nothing in the Carpenter case, 10 Cal. 2d 307, *supra*, indicative of a thought that the two companies were one and the same, at least after December 4, 1936. The entity of a corporation cannot be disregarded unless it be alleged and proved that the organization thereof was fraudulent or prompted by dishonesty and that injustice would be done if the corporate entity were not disregarded, and that there has been a cessation of the individuality and separateness of the corporation and the owners of its stock. (Judelson v. American Metal Bearing Co., 89 Cal. App. 2d 256, 262-263 [200 P. 2d 836], and cases therein cited.) Nothing of such a nature herein appears. The New Company was not an agency of the Insurance Commissioner subsequent to December 4, 1936, but even if it was, obvi-

ously such would not make the New Company the same as the Old Company.

Next we consider the claim of appellants that the directors of the New Company had no knowledge of the data on which the Plan of Mutualization was based, and in purporting to adopt the plan, acted as rubber stamps. Section 11525 of the Insurance Code provides that a Plan for Mutualization of a solvent insurance company may be carried out "by complying with the requirements of this chapter." One requirement is that the plan shall be "adopted by a vote of a majority of the directors." It is conceded that this was done on May 5, 1950. No authority is cited for the proposition that directors' action, once taken, can be attacked on the ground of insufficient information, and there probably is none, for obvious reasons. In fact, the law is, no doubt, to the contrary. (6 Fletcher, Cyclopedia of Corporations, p. 296.) Furthermore, there is no merit in the statement that the directors were not adequately informed. Prior to April 13, 1950, each director had received a copy of the report of the Price Determination Committee and of the Plan of Mutualization. Furthermore, at its meeting on May 5, the Board received reports, heard the testimony of informed witnesses, all to the effect that the plan could be practically accomplished, having due regard to the interests of all persons interested in the New Company, that it was based on sound principles, was fair, just, equitable, financially feasible, and that the price to be paid and the terms of payment were reasonable and fair; all of which seems to be a complete answer to this point raised by appellants.

We now take up the claim that no valid approval of the Plan of Mutualization has ever been given on behalf of the stockholders, the consent purportedly given by the conservator in the Rehabilitation Agreement did not consti-

tute a valid approval of the present Plan of Mutualization, and the liquidator or conservator could not delegate his power to the Price Determination Committee. The facts of this case take it out of the general rules of law enunciated in the authorities cited by appellants. Here, the validity of the rehabilitation agreement, wherein the conservator, for himself and his successors in interest, as shareholder of the New Company, consented and agreed to consent to such Plan of Mutualization as might be promulgated by a duly appointed Price Determination Committee, is, as is all other parts of said agreement, *res judicata*.

Thus, the proposition is not where a trustee, having certain duties to perform, on his own initiative delegates his authority or duties to another; rather is it a case where he is bound, both by contract and decree, to consent to what another may do. He could not have refused to give his consent, had he wanted to, under the facts in this case.

We in no way intend to detract from the force of the foregoing conclusion in adding that agreements in which obligations depend on fact determinations thereafter to be made by third persons are valid and not unusual. There are many cases so holding. Illustrative thereof are: Bewick v. Meacham, 26 Cal. 2d 92, 97 [156 P. 2d 757, 157 A. L. R. 1277]; American-Hawaiian Engineering & Const. Co. v. Butler, 165 Cal. 497, 513 [133 P. 280, Ann. Cas. 1916C 44]; Roberts v. Security T. & S. Bank, 196 Cal. 557, 568 [238 P. 673]; Silva v. Mercier, 33 Cal. 2d 704, 708-709 [204 P. 2d 609]; Market Street Ry. Co. v. Hellman, 109 Cal. 571 [42 P. 225]; 3 Williston on Contracts, page 2247, section 800.

Another contention of the appellants is that the conservator or liquidator could not give his approval as trustee for the shareholders until after the adoption of the

Plan of Mutualization by a vote of a majority of the board of directors, they specifically saying that the steps required to mutualize a solvent or delinquent corporation must be taken in the order enumerated in section 11526. We cannot agree. The section could easily have so provided, but it does not, except in subdivision (e) thereof, and we are not permitted to judicially legislate.

Also, if there could be any question about it, the fact that the language appearing in subdivision (e) is not made to apply to subdivisions (a), (b), (c), or (d) is strongly persuasive that the Legislature did not intend that such provisions should apply to these other subdivisions. (Market Street Ry. Co. v. Hellman, 109 Cal. 571, 587 [42 P. 225]; Estate of Bull, 153 Cal. 715, 717 [96 P. 366]; In re Sekuguchi, 123 Cal. App. 537, 538 [11 P. 2d 655]; 23 Cal. Jur. 762.) At any rate, if the liquidator was the stockholder whose consent was required, his consent will be deemed to have been given at the proper time, because being bound by the conservator's agreement to consent, equity will regard that as done which should have been done. (Civ. Code, § 3529; Poultry Producers of Central Calif. v. Nilsson, 197 Cal. 245, 254 [239 P. 1086].) It is wholly proper that substance should prevail over mere form.

Appellants complain that the Insurance Commissioner, prior to approving the Plan of Mutualization, did not conduct the type of hearing required by section 11527 of the Insurance Code. This is based principally upon the claim that the Insurance Commissioner did not have, or receive, proper evidence to justify his conclusion which approved the Mutualization Plan. The basic problem for the commissioner to determine was whether or not the price and terms of payment for the New Company stock were fixed in accordance with the rehabilitation agreement, for if they were, the Plan of Mutualization is fair and equitable

because it gives the stockholder the price and terms he agreed to take.

The point is made that some of the witnesses who testified before the commissioner were interested witnesses. Such claim could go only to the weight of the evidence and not its admissibility. It does not appear here, in any event, that any evidence received by him was not trustworthy, nor that any committeeman or valuer or any witness was guilty of partiality, bad faith, or misconduct in their appraisals or testimony. Therefore, the point cannot be upheld. (Cecil v. Bank of America, 107 Cal. App. 2d 38 [236 P. 2d 408]; Riccomini v. Pierucci, 54 Cal. App. 606, 608 [202 P. 344].)

Another point raised by the appellants is that they have been deprived of substantive due process because the stock of the New Company was valued as of the present, that the time of payment was fixed long in the future, payment was conditional, there was no provision for reasonable interest, and the price paid was grossly inadequate. On this question of due process we should never lose sight of the fact that the commissioner's approval of the Plan of Mutualization did not have the effect of taking appellants' property, since it was nothing more or less than a permit and did not compel the life policyholders to approve the plan, nor the stockholder to dispose of the stock as therein provided, or the New Company to adopt the plan. Even after the commissioner's approval the life policyholders could have rejected the plan, had they so desired. The stockholder could have rejected the plan but for the Rehabilitation and Reinsurance Agreement, which obligated the stockholder to dispose of the stock at the price and upon the terms fixed by the Price Determination Committee. The compulsion upon the stockholder flows from the obligations of the Rehabilitation and Reinsurance Agreement and not from the commissioner's approval of the

plan. Even if this were not so, we do not believe the point raised is sound. As we read the evidence it does not necessarily lead to that conclusion; in fact, it could well lead to a contrary conclusion, the one that was adopted by the Insurance Commissioner and upheld by the lower court, to wit, that the plan was fair and equitable.

This already lengthy opinion must come to a conclusion. We have carefully read the briefs of all parties and each point raised by the appellants. Those not hereinabove discussed, we find to be without substantial merit.

The record shows that the commissioner's order approving the Mutualization Plan was not improper, on the evidence submitted. As above indicated, the liquidator was bound by the rehabilitation agreement to dispose of the stock of the New Company on the terms fixed by the committee. Petitioners were parties to the proceeding in which the rehabilitation agreement was proposed, and their representatives participated in seeking that approval. They may not now complain of its terms.

The evidence before the commissioner was fully documented with respect to all factual data, the witnesses who testified appear to be outstanding in their fields, and their expert judgment on questions of valuation and valuation methods, interest rates and trends, and all other matters within the province of expert opinion, could not be disregarded on the basis of "mere unsupported suggestions and opinions as counsel." In that situation the commissioner could clearly have come to the conclusion that the plan should be approved.

We have studied this case diligently in an effort to ascertain if there was error committed in the court below. We can find none of any consequence.

The oral argument of this case was regularly set for hearing by this court for February 10, 1954. On February

1, 1954, the parties hereto signed, and on February 8, 1954, filed herein a stipulation waiving oral argument and agreeing that the case "may be submitted for decision upon the briefs and record on file." On February 10, 1954, appellants appeared before the court and made an *ex parte* application to have the court consider a purported agreement between Old Company and one Clint W. Murchison, wherein the latter agreed, subject to a number of highly important contingencies, to pay $17,000,000 for stock in Old Company.

Various briefs have been filed herein, mostly by *amici curiae*, respectively approving and opposing such application. We have concluded we may not give consideration to such agreement. (Redsted v. Weiss, 71 Cal. App. 2d 660, 666 [163 P. 2d 105]; Bassett v. Johnson, 94 Cal. App. 2d 807, 812 [211 P. 2d 939].)

If we were to give full consideration to the offer, as made, we would be in no position to hold that the Insurance Commissioner erred in his conclusions, since such evidence could, at the most, to be merely cumulative. (Katenkamp v. Union Realty Co., 36 Cal. App. 2d 602, 621-622 [98 P. 2d 239].)

And, in any event, such additional evidence obviously would not be "so conclusive that it compels the direction of a judgment in favor of appellant," nor would its effect upon this appeal be "decisive." (Bassett v. Johnson, *supra.*)

While the last 18 years' history of this company is no proof thereof, nevertheless, it is a well recognized principle that all litigation must sometime come to an end.

The judgment of the lower court must be, and is, affirmed.

Dooling, J., and Kaufman, J., concurred.

APPENDIX C

Opinion of the Superior Court for Los Angeles County



APPENDIX C

Opinion of the Superior Court for Los Angeles County

In the Superior Court of the State of California in and for the County of Los Angeles.

The Pacific Mutual Life Insurance Company of California, etc., et al., petitioners, vs. Wallace K. Downey, etc., et al., respondents. No. 579,832.

Filed March 24, 1952.

Memorandum of Decision

By this proceeding petitioners seek to review and set aside the order of the Insurance Commissioner approving a plan of mutualization of Pacific Mutual Life Insurance Company (hereinafter called New Company).

The factual and historical background, so far as is necessary to understand the numerous questions raised by petitioners, is as follows:

In 1936 Pacific Mutual Life Insurance Company of California, hereinafter referred to as Old Company, became insolvent. In July of 1936 the Insurance Commissioner, in accordance with the provisions of Section 1011 of the Insurance Code, filed an application for an order appointing him Conservator of Old Company. Pursuant to this application an order was made appointing the Commissioner as Conservator of Old Company, and vesting in him title to all the assets of that Company.

At the same time the court made an order which, among other things, authorized the organization of New Company, a respondent herein. In accordance with the order, the Commissioner organized New Company and transferred to it substantially all of the assets of Old Company, and received all of the stock of New Company, subject to the provisions of a rehabilitation agreement, which had been approved by the order last above mentioned.

It was thereafter found that Judge Edmonds, who had signed the order heretofore mentioned, was a policyholder in Old Company and was, therefore, disqualified, and that the orders he had made were void.

Thereafter a new application was made for the appointment of the Insurance Commissioner as Conservator, and this was heard by Judge Willis, and granted. Thereafter, upon notice, Judge Willis approved a rehabilitation agreement between New Company and the Insurance Commissioner as Conservator of Old Company. This agreement is in evidence in the present proceeding as Exhibit 9-A, and is hereinafter referred to as "Rehab" or "Rehab agreement".

In substance, insofar as the provisions thereof are pertinent in the present proceeding, the agreement provides that the Conservator should convey and assign to New Company all of the assets of Old Company, with certain exceptions; that New Company would reinsure the liability of Old Company and the Conservator under all insurance contracts issued by Old Company, except policies known as "non-can policies", which were policies of disability insurance issued by Old Company under which it had no right of cancellation so long as premiums were paid by the insured; that New Company would reinsure and assume the liability of Old Company and of the Conservator on all non-can policies, but at reduced amounts, varying from 20 per cent of the amounts payable under the face of the policy to 90 per cent of the amounts so payable; that if the Commissioner was appointed Liquidator of Old Company, New Company would pay to him an amount equal to the claims filed with and established against the Liquidator by such policyholders of Old Company as did not elect to accept reinsurance in New Company.

By paragraph 14 of Rehab it was agreed that New Company should, from time to time, transfer, from the

funds of New Company available for its general corporate purposes, to a special fund such amounts as New Company's board of directors should determine to be not reasonably required for the reasonable and proper conduct of the operation of New Company, and that the Commissioner, at the time of any examination of New Company by him, might require the transfer of additional funds to such special fund.

It was further provided that the moneys and assets from time to time placed in said special fund should be used by New Company to restore to the holders of non-can policies entitled thereto, benefits in excess of the amounts which were reinsured by New Company, to the end that the benefits "originally provided in said non-can policies as written may eventually be fully paid . . . with interest on deferred restoration payments . . . at the rate of three and one-half per cent . . ."

By paragraph 19 of Rehab it is provided that the Conservator or Liquidator should proceed in such manner and at such time as he thought proper, "subject to the provisions of paragraph 20 hereof", to realize upon the assets held by him; that the proceeds realized from the sale of any assets, other than assets received for the benefit of policyholders of Old Company who had rejected reinsurance by New Company, should be used by the Liquidator for the payment of any of his costs and expenses of administration and claims having preference in liquidation.

As to the balance of the amounts so realized, the agreement provides in part as follows:

> "(b) In the event benefits under Non-Can Policies shall not theretofore have been fully restored as provided in paragraph 14 hereof, a portion of the remaining proceeds (but not exceeding the amount required to provide complete restoration of the benefits under Non-Can Policies), in the ratio

which exists between the Non-Can Policies (evaluated as provided in subparagraph (b) of paragraph 17 hereof) whose holders have accepted reinsurance hereunder, and all Non-Can Policies (evaluated as provided in subparagraph (b) of paragraph 17 hereof), whether their holders have accepted reinsurance, or have rejected reinsurance hereunder, and have filed claims in the liquidation proceedings shall be paid to the New Company, and by it transferred to the special fund described in paragraph 14 hereof. . . .

"(c) Any portion of such proceeds remaining after making the payments described in subparagraphs (a) and (b) hereof shall be used to pay and discharge claims filed with the Liquidator and finally allowed.

"(d) Any portion of such proceeds remaining after making the payments described in subparagraphs (a), (b), and (c) hereof shall be paid to the New Company for the purposes of the special fund described in paragraph 14 hereof, to the extent the same may be required to provide full restoration of the benefits under Non-Can Policies.

"(e) Any portion of such proceeds remaining after making the payments described in subparagraphs (a), (b), (c), and (d) hereof shall be disposed of by the Liquidator in the manner provided by law."

Paragraph 20 of the agreement provides that neither the Conservator nor the Liquidator should dispose of any of the stock of New Company held by him, except in one of the manners provided for in said paragraph. It was then provided that at any time "between July 1, 1946, and January

1, 1948, and thereafter so long as the Conservator or a Liquidator of the Old Company may continue to hold any or all of said stock", 10 per cent of the holders of participating policies of life insurance might request New Company to create an appointing committee, which should consist of the holders of certain named designated offices, and that this appointing committee should then designate "a Price Determination Committee of not less than three and not more than five persons skilled in matters of insurance company valuation, which committee . . . shall determine whether in their opinion the proposed voluntary mutualization of the New Company . . . *can then be practicably accomplished, having due regard to the interests of all persons interested in the New Company.* If it be determined that such mutualization is not then practicable no further steps shall be taken in connection with a *possible mutualization* of the New Company under the provisions of this subparagraph until at least six months after the date of such determination."

It then provides that if in the opinion of the Price Determination Committee "mutualization is *then practicable,*" the Committee shall determine "the price to be paid upon such mutualization and appropriate terms of payment thereof", but that said determination should not be made prior to January 1, 1947.

The agreement then, after specifying certain items that should be taken into consideration by the Committee in determining the price to be paid, provides that the Committee shall, in its report to New Company, include a plan of mutualization of New Company, which plan should, in addition to any other relevant matters, specify "the price to be paid, the terms of payment, the persons by whom and the manner in which the right to vote the stock in New Company is to be exercised *pending complete* payment of the purchase price;" that the Committee "may provide in the

plan for the creation of a voting trust . . . designate the initial voting trustees and make provision for the appointment of their successors. Unless the benefits under Non-Can Policies have theretofore been fully restored and claims against the Liquidator fully paid, such plan shall further provide that such mutualization shall not affect the provisions of paragraph *17* or of paragraph *14* hereof, or the right of holders of Non-Can policies to the restoration of benefits from the sources and in the manner therein provided."

The agreement then requires that New Company, upon the request of 10 per cent of its policyholders entitled to vote, shall submit the plan "in accordance with the laws of the State of California then in effect." It then proceeds: "The Conservator for himself and for any successors in the ownership of said stock claiming under him in any manner other than through a sale of said stock pursuant to the provisions of subparagraph (d) *hereof agrees to consent and hereby consents* as the holder and owner of the stock of the New Company to such plan of mutualization. In the event said mutualization plan *is adopted* . . . Liquidator . . . *shall dispose* of such stock in accordance with such plan."

The agreement then gives to the Price Determination Committee, if appointed prior to January 1, 1948, the power to extend the time "within which mutualization may be effected hereunder for such period or periods of time as it may deem necessary for the orderly completion of mutualization proceedings as herein provided."

Subparagraph (b) of paragraph 20 provides a method of effecting a merger, consolidation, reorganization, or reinsurance of New Company, free from the effect of subparagraph (a) as to mutualization.

Subparagraph (c) gives Old Company the right, subject to the approval by the Court, to purchase from the

Liquidator the shares of stock of New Company held by him, by paying to the Liquidator an amount sufficient to complete restoration of Non-Can benefits and the payment of all claims against and liabilities of the Liquidator, subject, however, to the rights of policyholders as to mutualization if such payment be made prior to January 1, 1948.

Subparagraph (f) provides as follows:

> "(f) If the provisions of this paragraph 20, or of any one or more of the subparagraphs hereof, should be contrary to law or illegal or void, then such paragraph, subparagraph, or subparagraphs, shall be null and void, and shall be deemed separable from the remaining covenants and agreements in this agreement contained; and shall in no way affect the validity of any of the remaining provisions of this agreement."

In addition to approving the Rehab agreement and authorizing its execution by the Conservator, the order made by Judge Willis decreed that adequate provision is made by the Rehab agreement for each and every class of policyholder, creditor, and stockholder of Old Company, and "that neither said agreement nor the plan therein embodied" discriminated unfairly or illegally in favor of any policyholder, creditor, stockholder, or other person interested in Old Company, its property or assets, and that the "agreement and the plan therein embodied" and each did fairly and equitably protect and adjust the rights, obligations and liabilities of all persons concerned; that the Rehab agreement afforded "a feasible method of providing within a reasonable time full restoration of the benefits under the non-cancellable income policies" of Old Company.

By the order the Conservator was authorized "without further order of this court" fully and faithfully to perform all of the obligations and terms and conditions and

covenants on his part to be performed under the terms of Rehab agreement.

Paragraph 16 of the order provides:

> "That this court, without relinquishing by these specific provisions any jurisdiction by it retained as a matter of law, do, and it does hereby, specifically retain and reserve jurisdiction of the within proceedings for the purpose of authorizing or approving any act of the Insurance Commissioner of the State of California done, or to be done pursuant to or in accordance with this order, and for the purpose of making or entering, upon application of the Insurance Commissioner of the State of California or of Pacific Mutual Life Insurance Company, any order, decree judgment, or ruling required, permitted, or requested to be done, made, or entered in connection with or pursuant to the terms of said agreement, or for the effectuation of the purposes thereof."

By paragraph 19 the Conservator and New Company were authorized to do all things necessary, desirable or proper to carry out the terms of Rehab or to effectuate its purposes.

From this order certain policyholders of Old Company appealed, and on the appeal the order was affirmed. (See *Carpenter* v. *Pacific Mutual Life Ins. Co.*, 10 Cal. 2d 307).

In 1937 an order was made directing the Insurance Commissioner to wind up and liquidate the business of Old Company and appointing him Liquidator. From this order an appeal was taken by certain policyholders, and on the appeal the order was affirmed. (See *Carpenter* v. *Pacific Mutual Life Ins. Co.*, 13 Cal. 2d 306.)

In 1938 the Liquidator transferred the stock of New Company to five voting trustees, pursuant to the provisions

of Section 1037(e) of the Insurance Code enacted in 1937. Thereafter the Insurance Commissioner and certain policyholders sought orders directing the New Company and the voting trustees to retransfer the stock to the Liquidator upon the grounds that the transfer to the voting trust was invalid. From the order denying these applications an appeal was taken, and on this appeal the order of the Superior Court denying the relief sought was affirmed. (*Caminetti* v. *Pacific Mutual Life Ins. Co.*, 22 Cal. 2d 344.)

Since 1936 all claims of policyholders who did not elect to accept reinsurance in New Company have been paid the principal amount of their claim without interest, but still claim interest against the Liquidator (their claim for interest as against New Company having been denied) to an amount of approximately $500,000. In said period New Company has restored to the holders of Non-Can policies which were reinsured by New Company 36 per cent of the amount by which the policies had been written down on reinsurance.

In 1946 New Company, in compliance with a request made by its policyholders, pursuant to paragraph 20 (a) of Rehab, created an appointing committee, and in January, 1947 the appointing committee created a Price Determination Committee composed of Horace R. Bosforth, Albert J. Hettinger, Jr., Ray D. Murphy, and Alva J. McAndless.

In April, 1950 the Price Determination Committee made its report to New Company. By this report they stated that they answered in the affirmative the question "whether in their opinion the proposed voluntary mutualization of New Company . . . can then be practicably accomplished, having due regard to the interest of all persons interested in the New Company," and attached as a part of their report a plan of mutualization of New Company.

Thereafter the Board of Directors of New Company passed a resolution adopting the plan submitted by the Price

Determination Committee, and the voting trustees, without examination into or passing upon the merits of the plan or the sufficiency of the price to be paid by New Company for its stock, approved the plan. The plan was not, after its submission by the Price Determination Committee, approved by the Liquidator.

New Company submitted the plan to the Insurance Commissioner for approval, and after an extended hearing the Commissioner made his order approving the plan, and found that it protected the rights and interests of New Company, its policyholders and shareholders, and that it would be fair and equitable in its operation. It is this order which the petitioners, who are Old Company, and a committee of its stockholders, seek by this proceeding to review.

It may be noted here that none of the policyholders of New Company, nor any of the persons who hold claims against the Liquidator for interest, are parties to the proceedings in this court, or complain of the plan or the order of the Commissioner.

In substance, the plan submitted by the committee and approved by the Commissioner provides that the shares of New Company now held by the statutory voting trustees shall be immediately transferred to nine voting trustees, named in the plan (including the Insurance Commissioner), to be held by them subject to the terms and provisions set forth in the voting trust agreement, a form of which is annexed to and made a part of the plan; that the price to be paid by New Company for its shares is 3 million dollars, with simple interest at an annual rate equal to the highest coupon rate of United States Government bonds at the furthest maturity outstanding at the close of the preceding calendar year, plus $250,000 for each full calendar year by which the date of complete restoration of Non-Can benefits antedates December 31, 1973.

That this sum shall be paid by New Company at such time as, (a) the benefits to all Non-Can policies reinsured by New Company shall have been completely restored, (b) the funds standing in a special surplus fund to be created, plus the capital and surplus standing in general corporate accounts, equal or exceed the price of the shares, with interest as specified above; (c) that the financial condition of the Company is such that, after paying for the shares, it shall have admitted assets in excess of its liabilities equal to the amount of four per cent of all of its admitted assets, plus 25 per cent of the premiums collected during the preceding calendar year on all group insurance written on a one-year term basis and all accident and health insurance.

That there is to be set aside in a special fund, to be used in part payment of the purchase price, 5 per cent of the net profits of the Participating Department of New Company.

That in the event the price of the shares shall not have been paid by December 31, 1983, the plan shall be considered to have failed, and the voting trust shall terminate, the shares be returned to the Liquidator, and the amount standing in the special fund shall revert to the general surplus of the Participating Department of New Company.

It will serve no useful purpose to set forth here a synopsis of all of the evidence received before the Commissioner, but it is necessary to state the substance of a portion of that evidence, in order that certain questions raised, and my ruling thereon, may be clear.

Two members of the Price Determination Committee and one of the actuaries employed by the Price Determination Committee testified at length as to the manner in which, and the basis upon which, the committee arrived at the price to be paid by New Company for its stock when it consummated the proposed plan of mutualization. In

substance they testified that they had, by long and exhaustive actuarial studies, determined the amount necessary to fully but gradually restore the benefits of the Non-Can policyholders; that they had then discounted these amounts at 3 per cent interest to their present value, and found that the present value of the amounts necessary for restoration was 22 million dollars; that by similar studies they had established the probable earnings of New Company for each year, commencing with the year 1949 and extending to the year 2000; that by discounting the earnings for the years 1949 to 1974 (both inclusive) at 3 per cent (only a portion of the earnings for the last year were so discounted), they determined that the Company would be able to complete restoration of Non-Can benefits in the year 1974; that after the completion of restoration the stockholders of Old Company would be entitled to its earnings, and that the present value of these earnings from 1974 to perpetuity, discounted at 10 per cent, was $2,614,000; that by reason of the terms of the rehabilitation agreement it was necessary to add $500,000 to this amount, but that as certain risk elements had been disregarded, they thought it proper to deduct the sum of approximately $100,000, giving a present value to the stock of 3 million dollars; that the calculated earnings upon which their estimate of the time within which to complete restoration of Non-Can benefits could be made, and upon which they based the present value of future earnings, were net earnings, after provision for contingency reserves.

They further testified that in their opinion a buyer could be found who would be willing to presently pay 3 million dollars for the stock of New Company and await the right to participate in the earnings of New Company for 25 years; that the stock of large life insurance companies currently sold at 4.3 to 7.8 times of their estimated earnings after the deduction of voluntary reserves; that if the estimated earnings of New Company from 1948 to

perpetuity were discounted to their present value at 10 per cent, that value would be less than the amounts necessary for full restoration, and there would be nothing left for the stockholders; that if the present value of the stock were fixed by giving a value to the nonparticipating life insurance in force at 20 dollars per thousand, the value of the stock would be less than the amount necessary for restoration, and that, in their considered opinion, the price of 3 million dollars was a fair one to be paid to the stockholders.

They further testified that because the payment of the present value of the stock as determined by them was not to be made immediately, but was to be deferred, that they had provided for the payment of interest upon the 3 million dollars, and instead of fixing a rate of interest had used the basis of the highest coupon rate paid on long-term Government bonds, as they thought that would be equal to the amount New Company could earn upon the deferred payment from year to year; that they recognized that if restoration was completed sooner than they estimated, that is, prior to 1974, this would give an added value to the stock, and that they believed $250,000 for each year by which the date of restoration preceded 1974, was a fair estimate of the increased value.

There was introduced into evidence the report of the actuaries who had made the studies upon which the cost of restoration and future earnings were based, and in which the method and the data used are set forth in detail. (Exh. 28).

Petitioners attack the order of the Commissioner and the plan of mutualization from many angles, but before passing on points made by them, there are certain questions which, to a large extent, underlie most of the points raised by them, and which must first be disposed of.

At all times we must keep in mind the nature of this proceeding. I have heretofore ruled, and again rule, that

in this proceeding the court is not entitled to exercise its independent judgment as to any issue of fact, but must affirm the order of the Commissioner and deny the peremptory writ of mandate sought by the petition, if the Commissioner had jurisdiction, if there was a full and fair hearing before him, held in the manner fixed by statute, and if, viewed in the light of the whole record, his order is supported by substantial evidence.

Petitioners contend that before the Commissioner would have jurisdiction to hold a hearing or to make any order, the plan of mutualization submitted to him must first have been adopted by the Board of Directors of New Company and consented to by the Liquidator as the beneficial owner of all of the shares of New Company.

Respondents contend that these are not essential to the jurisdiction of the Commissioner, and that the Commissioner may make an order approving of the plan before it is adopted by the Board of Directors of New Company, or before any assent to it is given by the shareholders.

Commissioner's power to act is purely statutory, and he did not have the power to make the order here under review unless the statute, Section 11526 of the Insurance Code, was substantially complied with. That section specifies four steps that must be taken in the adoption of a plan of mutualization. They are: (a) Adoption by a vote of the majority of the directors of the corporation to be mutualized; (b) Approval by a vote of the majority of the outstanding shares of the corporation, or the written consent of such shareholders; (c) Submission to and approval by the Commissioner; (d) Approval by a majority vote of all the policyholders of the class or classes for whose benefit the stock is to be acquired and who cast their vote; (e) Filing in the office of the Insurance Commissioner after steps (b), (c), and (d) have been taken.

I am of the opinion that the Legislature intended that the steps set forth should be taken in the order named, and

this is the construction placed on the plan by the Commissioner and by respondents prior to the sufficiency of the consent by the shareholder having been raised in this proceeding. (As to the Commissioner's construction of the statute, see Transcript, Volume I, page 3.)

If any other construction is placed upon the section, it would serve no purpose. Until a plan is adopted by the corporation, there is nothing for the stockholders to vote upon. Until a majority of the stockholders have approved a plan submitted by the corporation, there is no plan which could be submitted to the Commissioner. If a plan were promulgated by the Company and then taken to the Commissioner and, after he had acted so as to approve the plan, the shareholders refused to approve, the Commissioner's action would have been futile and useless, and it would be necessary for him again to pass on a plan to which a requisite number of shareholders had agreed. If the plan were first submitted to the policyholders and then to the Commissioner, and later either the directors or the shareholders refused to approve, again his action would have been useless.

Certainly this section contemplates that there must be some agreement between the parties who will be bound by the plan, if it be approved, before the Commissioner is called upon or authorized to approve or reject it. I hold, therefore, that unless under the facts shown by the record, the shareholder did approve the plan prior to its submission to the Commissioner, he was without jurisdiction to act thereon.

Petitioners contend that the order made by Judge Willis in the liquidation proceeding is not a final order, and is, therefore, not res judicata, but that that order and the Rehab agreement are both subject to collateral attack in this proceeding.

The point is not well taken. The proceeding in which the order was made (to which I have referred and will refer to as "liquidation proceeding") was one authorized and had under Section 1043 of the Insurance Code. It was not an ex parte proceeding, but an adversary one. It was upon notice, and Old Company, one of the petitioners herein, and certain of its stockholders, appeared.

In that proceeding, Conservator, by his petition, sought authorization from the court to execute the Rehab agreement and directly tendered the issue as to the validity of that agreement, and each of its terms and conditions.

The order not only approved the agreement and authorized its execution by the Conservator, but directly adjudged its validity and fairness.

Every attack made by petitioners here upon the Rehab agreement and the order approving it could have been made in the liquidation proceeding.

The proceedings had under Section 1043 of the Insurance Code is the method provided by statute for securing an adjudication of the validity of a plan for rehabilitation. The order made approving such plan is a final, not an interlocutory order. Until the order is made the plan is not a binding agreement. When it is made, the plan becomes an effective agreement between the parties. An order approving the plan gives life to it. An order rejecting a plan kills it. The proceedings and the order made were not preliminary. They were the final step taken by the Conservator in rehabilitating the business of Old Company.

I hold, therefore, that neither the validity of the plan nor of the order approving it may be attacked in this proceeding. In view of this, it is unnecessary to pass upon many questions raised by the parties here.

Petitioners contend that inasmuch as Rehab did not set up a plan of mutualization, the court by that order did not

pass upon the question as to whether or not the present plan of mutualization approved by the Commissioner was feasible, reasonable, fair, or equitable.

It is quite true that the court in the liquidation proceeding did not act or pass upon any plan of mutualization. The court in the liquidation proceeding did not have, and has not now, jurisdiction of mutualization proceedings. That jurisdiction is vested in the Commissioner, subject to limited review in this proceeding. The court in the liquidation proceeding did have jurisdiction to pass upon the validity of the plan of rehabilitation set forth in the agreement before it, and the provisions of Section 20 of that agreement are an integral part of the plan that it approved and found valid.

Petitioners further contend that the court in the liquidation proceeding did not determine the validity of Section 20 because of the severability of clause (subparagraph (f) of that paragraph) which has been heretofore quoted. They assert that the provisions of subparagraph (f) of paragraph 20—that if any paragraph or subparagraph should be "contrary to law or illegal or void", then said paragraph or subparagraph should be deemed separable from the remaining covenants and in no wise affect the validity thereof—as the grant of a continuing right to any interested person to at any time attack the legality of paragraph 20 or any proceedings had thereunder. They assert that as the order of Judge Willis approved all of the terms and conditions of the rehabilitation agreement, it approved subparagraph (f) and therefore continued it in effect.

I think they misconstrued the purpose of subparagraph (f). The purpose thereof was undoubtedly to enable the court in the proceeding had for the approval of Rehab either to approve the plan as a whole, or if it believed certain portions of paragraph 20 to be illegal, then to approve it with those parts deleted. In other words, the petitioners

there said to that court: "We ask you to approve this agreement as a whole, but if you cannot give your approval to it as a whole, we ask you to approve it, after deleting therefrom such portions of paragraph 20 as you find contrary to law."

They thus submitted to the court by their petition the validity of all of the terms and conditions of paragraph 20, and when the court gave its approval of the agreement, without finding any provision of paragraph 20 to be contrary to law, it, by its judgment, established the validity of each of the provisions of that paragraph, and it became an integral part of the approved agreement; subparagraph (f) had then served its purpose.

Petitioners next contend that by paragraph 16 of its order approving the rehabilitation agreement, the court reserved the right to pass upon any plan of mutualization which might be thereafter submitted pursuant to paragraph 20 of Rehab and upon the fairness of the price to be paid for the stock of New Company under such plan.

The court in the liquidation proceedings had no jurisdiction, and does not now have jurisdiction to pass upon any plan of mutualization. That jurisdiction is given by statute to the Commissioner of Insurance. The court in the liquidation proceeding, however, did have jurisdiction and was required to approve or withhold approval of any plan of rehabilitation, and it had jurisdiction to approve any transaction affecting assets in the hands of the Conservator or Liquidator. Its jurisdiction and its duties as to the rehabilitation agreement are fixed by Section 1043 of the Insurance Code. Its jurisdiction and its duty as to transactions involving assets in the hands of the Conservator are fixed by subdivision (d) of Section 1037 of the Insurance Code.

I think it is apparent that the court did not reserve jurisdiction to pass upon the feasibility, fairness, justness or equitableness of any future plan of mutualization presented in accordance with paragraph 20, or to pass upon the fairness of the price fixed by such agreement, but that it actually exercised its jurisdiction by approving Rehab agreement.

It must be remembered that inasmuch as the orders of Judge Edmonds were void, the Conservator's title to the stock of New Company was not vested until Rehab was approved and executed.

Paragraph 20 was an integral part of the rehabilitation agreement, and when that agreement was approved and the Commissioner executed it, he accepted title to the shares of New Company subject to the conditions set forth in paragraph 20, that is, to the right of New Company to acquire that stock through mutualization proceedings had in accordance with the provisions of that paragraph; and the situation is no different than if the stock he received had been preferred stock, subject to call at a price fixed.

Certainly, no one would contend that the Conservator or Liquidator of an insolvent insurance company would have to have the approval of the court to surrender preferred stock, which the court had authorized him to accept in exchange for other assets, upon that stock being called in accordance with its terms. When the court approved Rehab it approved a transaction by which the Conservator was obligated to dispose of the stock he received in exchange for the assets of Old Company in a certain manner and upon certain terms, and it thereby authorized him to consummate the transaction without further order.

If, however, it be assumed that the court must exercise the jurisdiction given it under Section 1037(d), it seems evident that the court did exercise that jurisdiction. Certainly, Rehab agreement involved assets of Old Company of

a market value in excess of $1000; certainly the provisions of paragraph 20 as to mutualization constituted a transaction involving the disposal of the only asset received by the Conservator in exchange for all of the assets of Old Company.

Petitioners argue, however, that, at the time Rehab was approved, the stock of New Company had no market value, and, therefore, they say the court could not then exercise its jurisdiction under 1037(d).

The answer to this argument is clear. In the first place, while the stock of New Company had no market value inasmuch as it was all held by the Conservator and as not subject to sale could have no market value, it did have an intrinsic value which could be measured approximately by the net worth of New Company. And certainly the statute does not preclude the court from giving approval of a transaction involving property which has no market value because not traded in but which has an intrinsic value in excess of $1,000. The court, in liquidation proceeding having acted in approving the transaction which is set forth in paragraph 20, exercised its jurisdiction under 1037d as well as under 1043.

This does not mean that the Commissioner was authorized by the court, or required by the rehabilitation agreement, to consent to any plan of mutualization that might be thereafter adopted by New Company and presented to him as the shareholder of that company. It only means that the court has approved his giving his consent to a plan of mutualization which conforms to the provisions of paragraph 20.

If the plan now presented does not conform to the provisions of that paragraph, then the Commissioner has not consented thereto and is not authorized to consent thereto, and the Commissioner had no jurisdiction to make the order in question. If it does conform, then the Commissioner has, by the terms of paragraph 20, given his consent to it, and

the voting trustees are obligated by the terms of the trust to give their consent, which they have done.

If the plan does not conform to paragraph 20, then the voting trustees do not have power to consent, for the Conservator by vesting them with legal title could not vest them with any greater right to consent than he, himself, had, and he had no power to give and consent to any plan other than one conforming to the provisions of paragraph 20, without first securing court approval of his action. As to whether or not the present plan conforms to the provisions of Section 20 will be dealt with later.

Petitioners further contend that the Rehab did not, and the plan of mutualization does, constitute a disposal of the stock of New Company; that the mutualization agreement must, therefore, be approved by the court; that the Commissioner must, therefore, secure the approval of the court before he can consent to it.

This contention is answered by what we have already said. It is true that the mutualization plan is an agreement providing for the eventual sale of the stock of New Company, and that it provides for the present transfer of the legal title thereto to certain named voting trustees. But this agreement is a part, or, we might better say, the end result, of the transaction which was approved by the court when it approved paragraph 20 of the rehabilitation agreement.

Petitioners next contend that the order approving the Rehab agreement was void in that the court did not have before it a justiciable controversy as to the fairness, etc., of the plan of mutualization.

As heretofore pointed out, the court in the liquidation proceeding never had jurisdiction of a plan of mutualization as such, but it did have jurisdiction to determine whether or not the Commissioner should agree in advance to abide by a plan promulgated in accordance with the pro-

visions of paragraph 20 of Rehab. It did give its approval of that transaction. It may have erred in so doing. It may have acted unwisely in so doing, but it had jurisdiction so to do, and its order cannot be attacked here.

Petitioners next contend that the court could not delegate its duty under 1037(d) to give or withhold approval of the price and the terms upon which the stock of New Company could be disposed of by the Commissioner. The answer to this contention is that the court did not delegate its duty. Its duty was to approve or disapprove the Rehabilitation Agreement which included a transaction involving a disposition of New Company's stock; this duty it exercised.

The Petitioners contend that paragraph 20 of the Rehab agreement is void because thereby the Commissioner delegated his statutory power to determine the price and the terms upon which the stock of New Company should be sold. This contention, of course, is answered by the fact that the order adjudging the validity of paragraph 20 is now final, and the agreement is, therefore, not subject to attack in this proceeding. But, it is further answered by a consideration of the powers vested in the Liquidator by the statute. The powers granted to the Conservator by Section 1037 are very broad, and he is required only to have a court approval of the transaction involving property of the estate of a market value in excess of $1,000. He is empowered to deal with property in his hands upon such terms and conditions as he may deem proper, subject only to court approval in the instance above mentioned. Certainly, this power is broad enough to encompass a transaction by which he grants an option to buy at a price and upon terms of payment to be fixed by third person or persons.

It is true that the Commissioner acts as trustee, and it has often been held that a trustee may not enter into

option contracts where the price and terms of payment are to be fixed by third persons, but in none of the cases which I have cited were the powers granted the trustees as broad as the powers granted the Liquidator by Section 1037.

Petitioners contend, however, that the Liquidator in the performance of his duties is declared by Section 1059 of the Insurance Code to be a public officer acting in his official capacity in behalf of the state, and from this they reason that in handling an estate in liquidation he is bound by the same strict rules as govern in the handling of public funds or property.

This is not a proper conception of the meaning of Section 1059. The purpose of the Legislature in enacting 1059 and declaring that the Liquidator in the performance of his duties should be deemed a public officer, was to make it clear that in acting as a trustee of an estate in liquidation, he was still bound by the provisions of Political Code Section 4295 insofar as the provisions thereof are applicable. These provisions are now set forth in Sections 6100-04 and 6110 of the Government Code. The conclusion I have come to is made clear when one considers the large discretion and extensive powers granted a liquidator by Section 1037, to which I have already called attention. In exercising these powers he acts as trustee of a private trust, not a public trust. He handles, not public, but private funds and property. His acts affect not the public, but the policyholders, stockholders and creditors of a private corporation.

The petitioners contend that the Legislature could not have granted the Liquidator power to delegate the powers granted to him by statute, and that, therefore, the power to delegate his powers could not be given by contract. These questions, like all others attacking the validity of the rehabilitation agreement, are foreclosed by the finality of the order approving the validity of that agreement.

Petitioners contend that the Liquidator could not give his approval of the plan of mutualization until after its

adoption by the directors of the Company. I think they are correct in this contention. However, by the terms of the rehabilitation agreement, he is obligated to give his consent, and equity will look upon that as done which ought to have been done.

Further, as the Conservator was bound to give his consent, so were the voting trustees, and they have consented. Ordinarily, voting trustees cannot give consent to the sale of stock, and thus destroy their trust, but where the trustor is bound to consent, and the trustees are so empowered, their consent binds him.

Here the voting trustees were obligated by the terms of the voting trust agreement to carry out the rehabilitation agreement, and as this agreement bound the Liquidator to vote the stock, so as to approve the mutualization plan—the reason which ordinarily requires the consent of the beneficial owner, to action by the trustees which will destroy the trust, is absent.

Petitioners next contend that the rehabilitation agreement is against public policy and void because it seeks by contract to mutualize New Company, contrary to the statutes as to mutualization of insolvent insurers.

They argue that New Company is but the alter ego of Old Company and but an agency of the Liquidator, and that, therefore, any proceeding for its mutualization must be had in accordance with the provisions of Section 1043-1062 of the Insurance Code. This contention is without merit.

On being appointed Conservator the Commissioner had the option of doing any one of four things: First, he could liquidate Old Company, or under Section 1043 of the Insurance Code, he could mutualize it, reinsure its business, or rehabilitate its business. He chose to do the last, and through it to accomplish partial reinsurance of the business of Old Company.

In carrying out his choice, he formed New Company and transferred all of the business of Old Company to it. After this transfer, Old Company ceased to be an insurer. It had no policyholders. It had no power to write insurance. It was merely a corporation that had been an insurer, in the process of liquidation. New Company was not, and is not, insolvent, and while under limited supervision of the Commissioner by the terms of the rehabilitation agreement, it is not now and never has been in his hands as Conservator or Liquidator. Since the approval and execution of the Rehab agreement, the Commissioner has not, either as Commissioner or as Conservator, or as Liquidator, possessed or had title to any of the assets of New Company. Rehab, and the order approving it, divested him of all right and title to the assets of New Company which had vested in him by the order appointing him Conservator.

No fraud is perpetrated by failure to pierce the alleged corporate veil of New Company, nor does recognizing it amount to a mutualization of an insolvent insurer through contract and in a manner not authorized by law.

New Company is a solvent insurer, and the only statutes that are applicable to its mutualization are the sections of Chapter 13, Division 2, Part 2 of the Insurance Code.

Petitioners further assert that the corporate entity of New Company must be disregarded and the agreement of mutualization treated as if it were one for the mutualization of Old Company, an insolvent insurer, because they say that if this is not done the Insurance Commissioner becomes a judge in his own case and is disqualified from acting pursuant to Sections 11526-7 of the Insurance Code.

The Commissioner as Liquidator has no personal interest in the property he holds. He is purely a statutory trustee. As such trustee he is a distinct juristic person from the person who acts as a statutory administrative officer.

Even if it be assumed that the Commissioner, acting as such, and the Commissioner, acting as Liquidator, is not two separate juristic persons, still the court should not pierce the corporate veil. The corporate veil is only pierced to avoid injustice. Here, if the veil were pierced and the New Company treated as insolvent, the effect of doing so would be disastrous. It is difficult to see how the corporation could be treated as insolvent and mutualized as an insolvent insurer without seriously affecting the transaction which it entered into as solvent insurer, without any approval of the court or commissioner.

Between the two situations, that of permitting the Insurance Commissioner to function as an administrative officer despite his interest as statutory trustee in the matter to be decided upon by him as Commissioner, and the evil that would result from treating New Company as an insolvent insurer, there can be but one choice.

The petition here alleges that certain members of the PDC have in the past had, through corporations or firms of which they were officers or members, business relationships with New Company, and that these relationships disqualified them to act as arbitrators (that is, members of PDC). Petitioners, by their briefs, have strongly pressed this matter.

The answer to their contention is threefold:

A. The parties, by Rehab, agreed that the appointing committee might choose the persons to act as members of PDC; they thus consented to the appointment of any person chosen in good faith by that committee, and no charge is made that it did not act in good faith.

B. The business relationships alleged (as admitted by the answer of New Company), are of such a character as would not, as a matter of law, disqualify the person from acting as a member of PDC.

C. No evidence was offered before the Commissioner upon this question, although the record shows that the Petitioners were then informed of the matters they now allege. The question is, therefore, not open for decision here.

What I have heretofore said disposes of all questions raised by the Petitioners, except two. These questions are:

First: Is the plan approved by the order of the Commissioner one such as is contemplated by the rehabilitation agreement and one, therefore, to which the Liquidator has, by the terms of the rehabilitation agreement consented?

Second: Are the findings of the Commissioner that the plan protects the rights of Old Company and its shareholders and that it will be fair and equitable in its operation, supported by substantial evidence in the light of the whole record?

I think both of these questions must be answered in the affirmative.

By the provisions of Rehab the parties submitted to PDC for determination the question of whether, in the opinion of the Committee, mutualization was then (at the time of its report) practicable. The Committee has answered this question in the affirmative and unless their decision was arbitrary, the parties are bound by that decision.

Petitioners contend, however, that the plan proposed by the Committee in and of itself demonstrates that the Committee's decision that mutualization if "then practicable" was arbitrary because they say the plan does not provide either for the present consummation of mutualization or for a process of mutualization under which New Company is unconditionally obligated to buy and the shareholders unconditionally obligated to sell upon terms definite as to price and time of payment, but only provides for a process of mutualization under which the consummation

of mutualization is dependent upon certain future contingencies.

Their point would be well taken if paragraph 20 of Rehab could only be interpreted as contemplating present consummation of mutualization or a contract which provided unconditionally for the purchase and sale of the stock of New Company by it upon terms definite as to price and terms of payment. Paragraph 20 is subject to the interpretation just stated and which Petitioners would place upon it, but that is not the only reasonable interpretation that may be placed upon it and is not the interpretation placed upon it by PDC or the Commissioner.

Paragraph 20 of Rehab, when taken by its four corners and viewed in the light of the circumstances that existed at the time of its approval by the Court in the liquidation proceedings and its execution by the parties, is reasonably subject to the interpretation that it contemplated the adoption of a plan of mutualization under which the consummation of mutualization might not only be delayed but might be contingent upon the happening of future events.

At the time Rehab was entered into the stock of New Company had no value and could not even have a potential value until such time as the operation of New Company had indicated the probability that it could from its trust earnings make restoration of Non-Can benefits. The parties, by their agreement, therefore, postponed the time at which mutualization might be proposed by the policyholders for approximately ten years. By their contract they did not provide that at the expiration of ten years mutualization should take place, but only that a plan for mutualization might then be adopted, if, in the opinion of a price determination committee, it could then be adopted, having *due regard for the interest of all persons interested in New Company.*

The terms of paragraph 20 clearly indicate that the parties contemplated that the plan presented by the PDC might provide for an extended process of mutualization. The surrounding circumstances and undisputed facts show that they must have contemplated that the consummation of mutualization under any such plan might be defeated.

Paragraph 20 outlines the plan that may be presented by PDC. It provides that the plan shall specify not only the price but the terms of payment, shall name the persons by whom and the manner in which the right to vote the stock is to be exercised pending the complete payment of the price; that it may to that end provide for the creation of a voting trust and shall not only designate the initial trustees but make provisions for the appointment of their successor. It expressly provides that a plan may be adopted before the restoration of Non-Can benefits, but that in that event that "such mutualization" (that is the mutualization provided for by the plan) shall not affect the right of holders of Non-Can policies to the restoration of benefits as provided for in the agreement.

If the parties had contemplated that any plan promulgated by PDC should provide for the immediate consummation of mutualization, there was no reason to make provision for the stock to be held by anyone pending the payment of the price fixed. There was no reason for the appointment of voting trustees or for the appointment of successors to the initial trustees. It is evident that the parties contemplated that PDC might present a plan which provided for a process of mutualization to occur at a future date. Further than this, the plan expressly contemplates the adoption of a plan before the restoration of Non-Can benefits, but it also provides that in proposing a plan the PDC were obligated to protect the interests of Old Company and its shareholders. It seems to follow that the parties

must have contemplated that any plan adopted before the restoration of Non-Can benefits would of necessity have to defer consummation of mutualization until after that event for otherwise any amounts paid to New Company would, under the provisions of paragraph 19 of the agreement, have to be applied to the restoration of those benefits, thus depriving Old Company and its shareholders of any benefit therefrom.

Restoration of Non-Can benefits could only be made out of the corporate earnings of New Company. If a plan were adopted before the restoration of Non-Can benefits, the consummation of mutualization under the plan would of necessity have to be contingent upon the corporate earnings of New Company being sufficient to make restoration. It follows that the parties must have contemplated that such a plan might be defeated if the earnings of New Company were insufficient to accomplish restoration within the time limited by the plan.

I think the interpretation of paragraph 20 I have just indicated is a reasonable one, and that I, therefore, should not and can not substitute my judgment for that of the Commissioner and the PDC. I hold, therefore, that the plan presented and passed upon by the Commissioner is one contemplated by the Rehabilitation Agreement and is, therefore, one to which the Liquidator has consented, and that the Commissioner had jurisdiction to make the order under review.

Petitioners contend, however, that the finding of the Commissioner that the plan protects the interests of Old Company and its shareholders is not supported by substantial evidence. They say it was the duty of the Commissioner to make his own determination from evidence of the value of the stock of New Company at the date fixed by the plan for mutualization and to determine whether or not the price fixed was, in view of that fact, a fair price. They say that

the Commissioner did not have any evidence before him from which the value of the stock of New Company could be determined as of the date fixed for the acquisition of that stock by New Company and the payment of the price, and that therefore the Commissioner's finding is not supported by substantial evidence.

It is undoubtedly true that it was the duty of the Commissioner to determine whether or not the plan protected the interests of the shareholders of Old Company, but it does not follow that it was his duty in the present case to look behind the report of the Price Determination Committee and make an independent determination of the value of the stock and the fairness of the price. In the present case the shareholders, by paragraph 20 of Rehab, agreed that the price to be paid for the stock should be fixed by the Price Determination Committee, and agreed to dispose of the stock at the price and upon the terms it fixed, and the committee, having fixed a price and the terms of payment, the shareholder is obligated to accept that price unless PDC acted arbitrarily. (There is no question of fraud or gross mistake involved.)

As the plan presented gives to the shareholder the price for which he has agreed to sell, it protects him, and the Commissioner was bound to so find unless the evidence disclosed that PDC acted arbitrarily in fixing the price.

The Petitioners contend that PDC did act arbitrarily. They point out that under the plan mutualization will not in fact occur for approximately 25 years, and that the PDC can not fix, and had no facts before it from which it could fix the value of the stock as of that time and that therefore it had no basis upon which to fix a price to be paid as of that time.

It must be conceded and Respondents do concede that neither PDC nor the Commissioner had any facts before them from which either the market value or the intrinsic

value of New Company's stock could be determined as to the time fixed for consummation under the plan. PDC was not, however, charged with fixing the value of the stock as of the date of consummation, but charged with fixing a price to be paid as of that date. "Price" in its broadest sense is synonomous with "value", but in its narrower and more common sense it means the amount of money to be given in exchange for something else, and I think it is in that sense that the word is used in paragraph 20 of Rehab.

PDC did fix that price. It fixed it at $3,000,000 plus simple interest and in certain events, other augmentations. Unless it acted arbitrarily in so doing, its determination of the price to be paid is final and binding upon the parties.

An arbitrary act or decision is one "arrived at through the exercise of will or by caprice, one supported by mere option or discretion and not by a fair or substantial reason." (*Bedford Investment Co.* v. *Folb,* 79 Cal. App. 2d 363, at 366.) The committee's decision was not such.

The facts which the PDC had before it, as shown by the record here, were sufficient to uphold findings that: the present value of the stock was not in excess of $3,000,000; that if that value were now paid (and New Company could pay it now from its present capital and corporate surplus and still remain solvent), Petitioners could receive no benefit therefrom; that if all the future earnings of New Company were discounted at a reasonable rate, their present value would be an amount insufficient to restore Non-Can benefits, and that, therefore, even if that value were fixed as the price to be paid and New Company were in a position to pay it, still Petitioners could receive no benefit; that the right of Non-Can policyholders to restoration was a prior charge upon all corporate earnings of the Company; that a present value of $3,000,000 was only justified if the earnings of New Company were sufficient to enable it to complete restoration of Non-Can benefits by the middle of 1974.

On the basis of these facts it cannot be said that the committee acted arbitrarily and without substantial reason in fixing the price and terms of payment. The committee was dealing not with ascertained facts but with future probabilities. It of necessity had to recognize that there was no certainty that the earnings of New Company would be such as the committee, on the basis of all the presently known facts, calculated they would be. In order to protect the rights of Petitioners they had to defer payment until New Company had been able to make restoration of Non-Can benefits. If the Company were able to make such restoration prior to the middle of 1974 (the date indicated by the studies of PDC), then the present value of $3,000,000 was too low, and the committee provided for such an event by adding to that price an augmentation of $250,000 for each full year by which complete restoration antedated December 31, 1973. On the other hand, if New Company should be unable to make restoration of Non-Can benefits until after 1974, the present value of $3,000,000 is too high, for in fixing that value the committee had assumed that the shareholder would be entitled to all earnings after that date. In this latter contingency, however, the plan does not provide for any reduction of present value, but places the risk of it on New Company. The committee could with reason have treated the benefit thus given the shareholder as a further compensation for the delay in payment.

The committee of necessity had to take the situation of all parties and all of the facts and circumstances in consideration in fixing a price, and in view of this we can not say that their conclusion as to the amount to be paid was not a rational one.

PDC might well have approached the problems presented to it and resolved those problems differently than they did. We may not agree with their approach or with

their reasoning, but we cannot say, nor could the Commissioner say, that they acted without reason, and neither the Commissioner nor this Court can substitute his or its reasoning for that of the committee.

I have arrived at this last conclusion reluctantly because of the fact that all the shareholder presently receives under the plan is a conditional promise to pay a sum of money at a distant date in the future and this promise has a present value, if the sum to be paid is discounted, for interest only, at 3%, much less than the sum which the committee finds to be the present value of the stock.

It follows that the petition for a peremptory writ of mandate must be denied and the alternative writ discharged. I find that the Commissioner had jurisdiction, that there was a full and fair hearing upon notice before him, and that his findings are supported by substantial evidence.

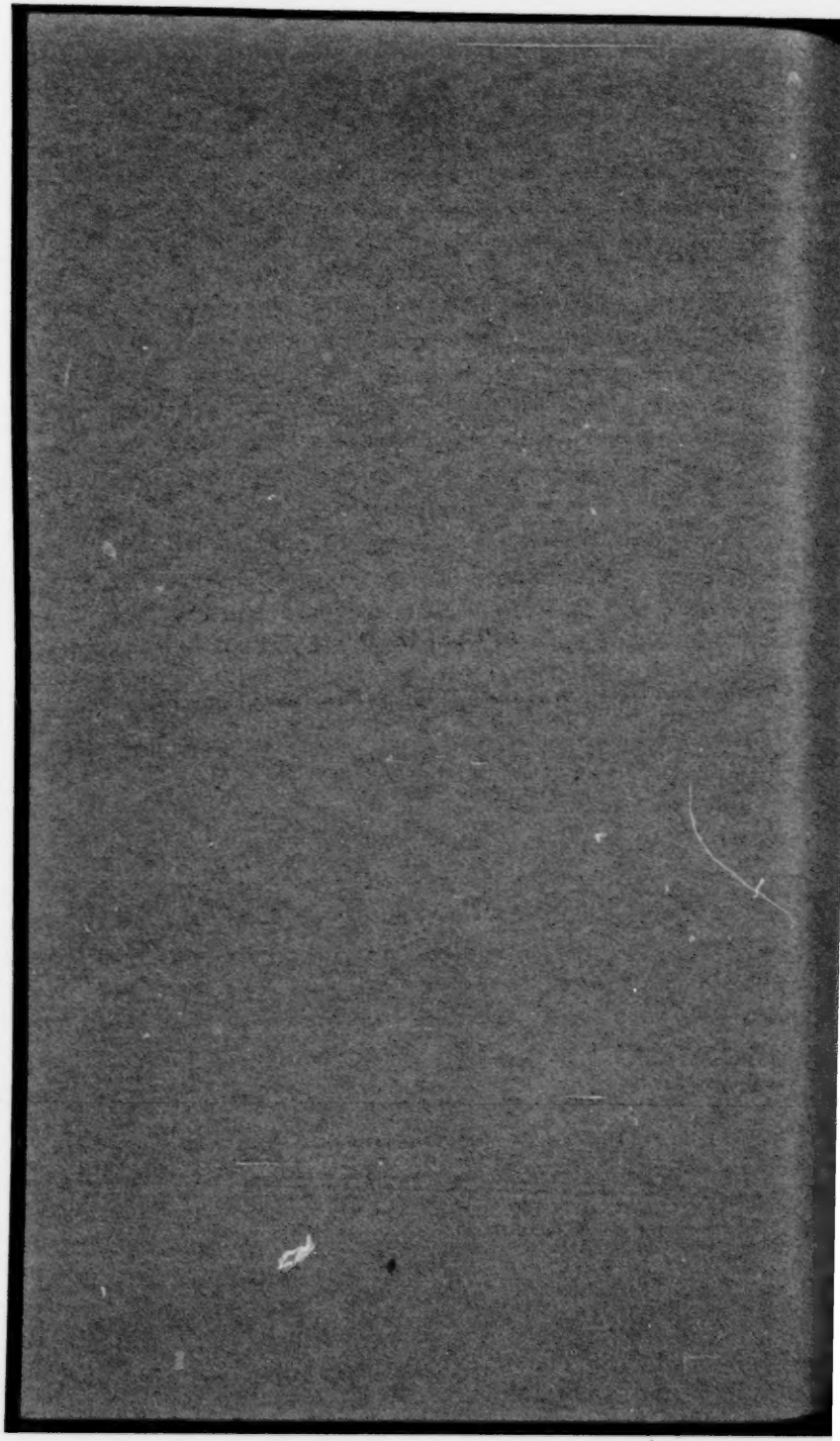
Counsel for respondents will prepare findings and judgment.

PAUL NOURSE
Judge.

March 24, 1952.

APPENDIX D

Opinion and Decision of the California Insurance Commissioner



APPENDIX D

Opinion and Decision of the California Insurance Commissioner

State of California, Department of Insurance

In the Matter of Pacific Mutual Life Insurance Company, a California corporation.

Opinion and Decision

BY THE COMMISSIONER

The Pacific Mutual Life Insurance Company of California (hereinafter called the "Old Company") is a California corporation. It was engaged in the life and disability insurance business for many years until misfortune overtook it in 1936. In 1918, or thereabouts, it had embarked upon a program of sale of policies of noncancellable accident and health insurance (hereinafter called "Non-Can"). It was this form of insurance that led to its insolvency, which resulted in its seizure by the Insurance Commissioner of the State of California in July, 1936.

Briefly, the non-can policies provided very broad disability indemnities for partial and permanent disabilities. With the exception of a few policies written just prior to the time the company was found to be insolvent, the non-can policyholders suffering permanent total disabilities became life annuitants with large indemnities under the terms of the contracts issued. The premiums on new policies were increased from time to time during the period this non-can business was written and the maximum benefits on such new policies were reduced during this time. Nevertheless, because all of the premiums at which the business was written were so low in comparison to the benefits granted, the company suffered huge losses. When reserves on the non-can business were required to be set up on a realistic basis, its capital and surplus were entirely wiped out and a very large deficit developed. The Old Company was thereupon

taken over by the Insurance Commissioner in conservatorship, and shortly thereafter in liquidation. Under the law then and now prevailing, the Insurance Commissioner of the State of California is the conservator or liquidator in the event of such proceedings being taken against an insurer authorized to do business in the State of California.

The Old Company wrote life insurance on a participating basis and also on a non-participating basis. It also wrote a very substantial volume of accident and health insurance on a non-participating basis. The assets devoted to the participating life business written by the Old Company were held separate and apart from the other assets of the company and, for most purposes, it can be said that this department was, in effect, a mutual company operated within the corporate framework of a stock insurer.

The Insurance Commissioner, at the time of the conservatorship, caused a new corporation to be formed, called Pacific Mutual Life Insurance Company (hereinafter called the "New Company"), under the laws of the State of California. Capital and surplus for the New Company were provided from the surplus of the Participating Department of the Old Company. The Commissioner, as Conservator, was the purchaser of the stock. The New Company fully reinsured all of the life insurance policies and all of the accident and health insurance policies of the Old Company, other than the non-can policies, under the terms of a reinsurance and rehabilitation agreement which becomes all-important in this proceeding. This agreement is hereinafter called the "Rehabilitation Agreement." Opportunity was given at that time for life and accident and health policyholders of the Old Company to refuse this reinsurance and file their claim against the Liquidator. A small number, only, of such policyholders ever filed such claims. Nearly all of them accepted the reinsurance in the New Company.

The non-can policyholders were given the option of accepting partial reinsurance or filing their claims against the Liquidator. Most of the non-can policyholders accepted the limited reinsurance and a relatively small number filed their claims. The earliest policies issued by the Old Company, because of the tremendous rate or premium deficiency pertaining to such policies, were reinsured to the extent of 20% only; the remainder were reinsured to a greater extent. The last group of such policies to be issued, wherein the rates charged and the benefits promised were on a more realistic basis, were reinsured to the extent of 90%.

The Rehabilitation Agreement provided that there should be restored to the non-can policyholders from time to time, out of certain of the profits of the New Company, the Benefits which were not reinsured. Under the terms of the agreement, the company was left free to make such restorations as it considered proper out of certain of its profits which are hereafter described, in any year other than a year in which the company was regularly examined by the Insurance Commissioner. In the years in which the company was so examined, the Commissioner was given power to require restorations out of earned surplus of the so-called Corporate Department of the New Company to such extent as he thought reasonable

The New Company was separated into several departments—the Participating Department, the Non-participating Department, the Accident and Health Department, and what was called the Corporate Department. The Participating Department was and is, in effect, a mutual life insurance company run within the corporate structure of the New Company, its assets being separated from the remaining assets and surrounded with safeguards maintained to prevent them from being used for the benefit of any but the Participating policyholders. The profits of this Department on business written directly by the New Com-

pany were not available for the restoration of the non-can policies under the terms of the Rehabilitation Agreement. 10% of the profits of the old (reinsured) Participating business under the terms of the Rehabilitation Agreement were available for restorations of the non-can business.

The so-called Corporate Department was really not a department at all, but was an accounting device set up to account for or hold the profits and surplus of the Non-participating Department, the Accident and Health Department and the 10% of profits of the reinsured participating business, referred to above.

It is obvious that the New Company was formed to prevent the tremendous loss that would have been incurred by all policyholders if it were necessary completely to liquidate the Old Company without any reinsurance.

Shortly after the New Company was formed and the Rehabilitation Agreement was executed, legal title to the stock was transferred to a group of voting trustees under the terms of a voting trust agreement. The trustees under the terms of this agreement voted the stock and thus controlled the New Company. The Insurance Commissioner, as Liquidator of the Old Company, however, retained, and still retains, the beneficial interest in such shares.

Since 1936 the New Company has been reasonably prosperous and as of the end of 1948 restorations of 24% had been made upon the originally uninsured portions of the non-can policies. Presently, a total of 36% has been restored. The Rehabilitation Agreement provides that simple interest at the rate of 3½% per annum shall be paid upon such restorations at the time they are made. The restorations made represent a very large sum of money.

The Old Company is a party to the Rehabilitation and Reinsurance Agreement because it was executed by the Commissioner as Conservator thereof. The agreement recognizes a contingent interest of the Old Company in

the New Company. It also recognizes a right of the policyholders of the New Company to propose that any or all of its departments be mutualized if possible, and made provision for a method of arriving at a plan for mutualization if it was found, by a committee provided for in the Rehabilitation Agreement, to be feasible. It also recognizes that the stock of the New Company may be sold if it becomes necessary for the protection of the estate in conservation or liquidation, the New Company or its policyholders. This sale can be made only after a proper showing of the necessity for such sale and a full hearing thereon.

These provisions are contained in Section 20 of the Rehabilitation Agreement, and since that section of that agreement is of paramount importance in the determination of this matter, that section of the agreement is set forth at length as Part I of the Appendix to this Opinion and Decision.

Pursuant to the provisions of Paragraph (a) of Section 20, and within the time allowed for such action, the required number of holders of Participating policies of life insurance requested the New Company to create an Appointing Committee with a view to a possible voluntary mutualization of the New Company. The Appointing Committee duly appointed a Price Determination Committee as provided in said Section 20(a). The members selected were:

Mr. Horace R. Bassford, Vice President and Chief Actuary of Metropolitan Life Insurance Company

Mr. Albert J. Hettinger, Jr., a partner of the firm of Lazard Freres

Mr. Ray D. Murphy, Vice President and Actuary, of Equitable Life Assurance Society

Mr. A. J. McAndless, an actuary by profession, and President of Lincoln National Life Insurance Company.

This committee accepted the appointment and elected Mr. McAndless chairman thereof. The committee entered upon its deliberations and after long and extensive studies rendered its report on April 4, 1950.

Thereafter, pursuant to the provisions of the Rehabilitation Agreement, the plan was submitted to all life policyholders of the New Company, who, by the required vote, requested that it be submitted. The plan was thereupon submitted to the Insurance Commissioner of the State of California for his examination, pursuant to the provisions of Section 11527 of the Insurance Code of this State. That section reads as follows:

> "11527. The commissioner shall examine the plan submitted to him under the provisions of subdivision (c) of Section 11526. He shall not approve such plan unless in his opinion the rights and interests of the insurer, its policyholders and shareholders are protected nor unless he is satisfied that the plan will be fair and equitable in its operation."

A public hearing was held in order to determine the questions required to be determined by the provisions of that section. The hearing went on for many days. Abundant testimony was taken, and documentary evidence was also submitted. The case was ably and thoroughly argued by counsel for the various interested groups.

The Price Determination Committee found that mutualization was feasible and formulated a plan for such mutualization. It found that the plan adequately protects the rights and interests of the New Company, of each class of its policyholders, and of all interests represented by the Insurance Commissioner of the State of California as holder of the beneficial interest in the stock of the New Company, and further found that the plan would be fair and equitable in its operation and that it could be prac-

ticably accomplished, having due regard to the interests of all persons interested in the New Company.

A copy of the plan for voluntary mutualization presented by that committee, excepting the voting trust agreement, is attached as Part II of the Appendix to this Opinion and Decision.

Greatly epitomized, the plan determined that both the Participating and Non-Participating Life Departments of the company should be mutualized by the purchase and cancellation of all of the outstanding shares of capital stock of the New Company, thus converting the New Company into a non-stock insurer conducted for the benefit of its members who shall be the policyholders of the participating and non-participating life classes.

The price to be paid for the outstanding shares is to be three million dollars with simple interest in each calendar year at the rate paid on the furthest maturity of United States Government bonds publicly held and quoted at the end of the preceding calendar year. This purchase price is to be augmented by the sum of two hundred fifty thousand dollars for each full calendar year by which the date of completion of restoration of non-can benefits antedates December 31, 1973. The same rate of interest under the plan will apply to the augmentations in price subsequent to the completion of restoration.

The plan provides for the accumulation of a fund to be used in partial payment of the purchase price and interest, by setting aside a special surplus fund of 5% of the net profits before dividends of the Participating Department exclusive of the profits from contracts reinsured under the Rehabilitation Agreement. This special surplus fund shall have interest upon it set aside in the fund at the same rate as interest is to be paid on the purchase price.

The purchase price is to be paid only after completion of full restoration of the non-can policies and when the

fund standing in the special surplus fund plus the capital and surplus in the general corporate accounts equal or exceed the price plus interest. The financial condition of the corporation also has to be such that after the payment, as aforesaid, the company shall have admitted assets in excess of its liability amounting to 4% of its admitted assets plus 25% of the premiums collected during the preceding calendar year on all one-year term group insurance business and on all accident and health insurance. The plan provides for a method of bookkeeping with respect to the special surplus fund and the effect of payment of the purchase price of the shares.

The plan also provides that the present method of restoration of non-can benefits, as set forth in the Rehabilitation Agreement, shall be continued.

Upon the acceptance by the policyholders of the plan, the present voting trust agreement shall be terminated and the legal title to the shares shall be held, pending the payment of the purchase price and cancellation, and shall be voted by another group of voting trustees named in the plan. The plan provides that it shall be the policy of the New Company to write at least half of its new life insurance other than group insurance each year in the Non-Participating Department. It provides for the doing of all acts necessary legally to accomplish the mutualization upon payment of the purchase price, and for the cancellation of the shares. It provides for an effective date of the plan and what shall be done in the event that it is impossible to consummate the mutualization of the New Company, and for the interpretation of the language in such a way that the provisions of the Rehabilitation Agreement shall be carried out.

CONTENTIONS OF THE VARIOUS PARTIES

The New Company itself was an active proponent of the plan at the hearing, as was an association of its general agents. Both the company and this association contended that the plan properly protects the rights and interests of the New Company, its policyholders and its shareholders, and that the plan would be fair and equitable in its operation.

The plan was opposed by an association of stockholders of the Old Company, which was called Pacific Mutual Shareholders Protective Committee (which is hereinafter referred to as the "Shareholders"), by a policyholder of the company, and by a group of non-can policyholders. Those who opposed the plan are hereinafter sometimes called protestants.

A letter, purporting to be an offer, was presented by American National Insurance Company, of Galveston, a large life insurance company, offering to purchase the stock of the New Company from the Commissioner, as Liquidator, for three million dollars. That company also offered to agree to restore benefits on non-can policies by the use of profits of the New Company or, if they proved insufficient, within seven years, out of its own funds. It also contained other stipulations which are unimportant here. It was received in evidence because it bore upon the reasonableness of the purchase price determined by the Price Determination Committee for said shares. Under the terms of Section 20(d) of the Rehabilitation and Reinsurance Agreement, this offer of purchase could not be accepted as the basis of a contract for the purchase of such shares, however, because such shares cannot be sold unless it is found that conditions are such as to require such a sale of stock for the protection of the estate in liquidation, the New Company or its policyholders. No such finding is possible on this record because it affirmatively appears that

of other life insurance companies similarly situated, its business would not have expanded, it would not have been prosperous, and without being prosperous it is obvious that restorations would have been greatly impeded. To use all of the profits of the New Company for restoration would have been only to call into play the ancient aphorism of killing the goose that laid the golden egg.

The evidence demonstrates that the surplus of the company has been allowed to grow and that the ratio of surplus to admitted assets has increased since the New Company began its operations. Whether the surplus should have been allowed to increase at a rate less than that which it has increased, is a question of judgment and discretion. If the management of the New Company, or the Insurance Commissioner, has abused that discretion, the remedy of protestants is not in this proceeding, but is in a proceeding in Court.

Protestants further contend that if the plan of mutualization is approved, the New Company would have an interest in deferring restoration payments, in order to minimize the amount which eventually would have to be paid for the stock of the company. The plan of mutualization does not in any way affect the provisions of the Rehabilitation Agreement with respect to restoration. The New Company is still bound to make restoration with reasonable dispatch and the Insurance Commissioner is enjoined by the terms of that agreement to see that any funds in excess of those reasonably needed by the New Company should be applied to restoration at the time when the company is officially examined. It must be assumed that future Insurance Commissioners will perform their duty in enforcing the terms of the Rehabilitation Agreement.

The Price Determination Committee has estimated that full restoration will probably be accomplished in about twenty-five years from the end of 1948. These protestants

contend that restoration by this method will be too slow, that it is contrary to the intent and spirit of the Rehabilitation Agreement, and that by the time full restoration is made, many—if not most—of the non-can policyholders will be dead. It is contended that if the mutualization plan is found not to meet the requirements of Section 11527 of the Insurance Code, other means may be found by which restoration can be completed much sooner than is contemplated by the authors of the plan of mutualization.

While restoration has been and remains a paramount consideration under the Rehabilitation Agreement, it must be remembered that when the policyholders of the Old Company, including the non-can policyholders, accepted reinsurance in the New Company, they became parties to novations and such policyholders bound themselves to accept the terms of the Rehabilitation Agreement. The non-can policyholders, by accepting such reinsurance, bound themselves to accept restoration in the manners contemplated by the Rehabilitation Agreement and in no others.

The contentions of protestants to the effect that the mutualization plan should not be approved, in order that other and more expeditious means of restoration might be developed, are not convincing. In the first place, there is no assurance that any better plan could be worked out and it is to be noted, again, that no such plan has been developed in something over fourteen years. In the second place, the provisions and safeguards contained in the Rehabilitation Agreement with respect to restoration are not in any way affected by the plan and, as stated above, non-can policyholders are not entitled as a matter of right to any other method of restoration.

It should be noted that the twenty-five year estimated period for full restoration is only an estimate. It is in no way binding on the Commissioner or on the company. Both will still have the duty to see that restoration is accomplished

at the earliest date possible, consistent with sound judgment as to the company's financial position.

Protestants contend that the plan does not meet the terms of the Rehabilitation Agreement because it provides for mutualization only of the Life Departments of the company with such departments controlling the Accident and Health Department as a proprietorship. This contention is answered by an understanding of what mutualization means. It means, according to the Insurance Code, Section 11525, the acquisition of the stock of a company by its policyholders for the benefit of its policyholders, or any class or classes thereof. The whole section reads as follows:

> "11525. A solvent domestic incorporated insurer having a paid-in capital represented by outstanding shares of capital stock and issuing, on a reserve basis, nonassessable policies of life insurance or of both life and disability insurance, may convert itself into an incorporated mutual life insurer, or life and disability insurer, issuing nonassessable policies on a reserve basis. To that end it may provide and carry out a plan for the acquisition of the outstanding shares of its capital stock for the benefit of its policyholders, or any class or classes of its policyholders, by complying with the requirements of this chapter."

The plan falls within this definition and therefore this contention of protestants is without merit.

Protestants further contend that the plan was unfair to the life policyholders of the New Company, particularly the participating policyholders thereof, because they, at the present time, are true mutual policyholders in that the Participating Department of the company is separate and apart from the other departments of the company and the assets thereof cannot be touched excepting for the benefit of the participating policyholders. It was pointed out in this regard

that the original capital and surplus funds of the New Company were provided by the Participating Department of the Old Company and that a percentage of the profits of the old participating business is available under the terms of the Rehabilitation Agreement for restoration. The plan provides that funds for payment for the stock under the plan must be provided by the profits of the Participating Department. This contention of protestants therefore requires serious consideration because, at first glance, at least, it appears to have very considerable merit.

With respect to the old participating policyholders, it was frankly stated by one group of proponents of the plan that mutualization as to the old participating policyholders would be of value to them mainly on a psychological basis, in that the turmoil surrounding the New Company and its predecessor would be ended. Thereupon, its agency force would overcome sales resistance because of a stabilization of the New Company's future. Also, all participating policyholders ultimately would have the benefit of the profits of the Accident and Health Department of the company, if any there were. These same considerations applied to the new participating policyholders who, as a class, are probably younger and hence have a better chance of surviving the time when full mutualization is accomplished.

The advantage of the plan to the non-participating policyholders is quite obvious in that they will ultimately become, if the plan is successful, proprietors of the company along with the other participating policyholders, and will not have to make payment for this interest. It should be remembered, in this regard, that Section 11527 does not require a plan of mutualization to be shown to be to the advantage of any particular class or classes of policyholders.

The accumulation of the fund for payment of this purchase price is restricted to a sum of 5% of the profits of

the Participating Department, before dividends to policyholders. It is well-known that mutual life insurers do not pay or return all of their profits to their policyholders as dividends, but customarily retain some portion of such profits, or as they are sometimes called, excess premiums, as additional surplus for additional protection to policyholders. This fund, by the terms of the plan, is still the property of the Participating Department, and a part of its surplus. When payment for the stock is made, and the company is mutualized, the general surplus of the New Company would be more directly available for the benefit of participating policyholders, and therefore there should be less need for a separate participating surplus than before. In any event, provision is made for return of monies paid from this fund. Thus, it is extremely unlikely that the 5% accumulation would in any way affect the dividends to the participating policyholders.

As has already been pointed out, restoration from profits as contemplated by the Rehabilitation Agreement will in no way be affected by mutualization, and if the evidence and contentions of the association of general agents of the company who appeared as proponents of the plan are believed, restoration may be hastened by adoption of the plan because it would be easier to sell insurance when all turmoil over control of the New Company is put to an end and the company embarked upon a business course on an even keel without threat of further business storms.

Protestants contended that the real advantage of this plan would be to the management of the New Company and that, it was said, it is well known that managements of mutual insurance companies tend to perpetuate themselves. This contention also is without merit. That there have been abuses in the mutual insurance field on the part of managements perpetuating themselves, cannot be seriously questioned but the same can be said of abuses of management of

all business corporations. Mutual policyholders are analogous to stockholders in many respects. It is well known that stockholders frequently are not diligent in protecting their rights in corporations in which they own the proprietary interest. They fail to attend stockholders' meetings or properly to interest themselves in the corporation's affairs. The law provides remedies for the abuses mentioned and if a stockholder wishes to avail himself of such remedy, he can do it. The law likewise gives such remedies to mutual policyholders. If they sleep upon their rights, they have no one to blame but themselves. It cannot fairly be said that because there have been abuses in the past in the perpetuation of management of some mutual insurance companies that such will be the case with respect to the company here involved. If such abuses should ever develop, it behooves the policyholders to remedy the situation in the manner provided by law for that purpose.

The contention is made by the Stockholders, particularly, and to a certain extent by the other protestants, that the value placed upon the stock by the Price Determination Committee and incorporated in the plan by them is unreasonably low. There was abundant evidence to support the findings of the committee as to the price of three million dollars, both upon the basis of a price to be paid for non-participating life insurance in force and upon other bases.

In arriving at the estimate of the value of the stock, the committee made a detailed study and estimate of the probable earnings of the New Company. Upon the basis of this estimate and assumed discount rate, the value of the stock was mathematically determined. The committee likewise considered the value of the business from the standpoint of the market value of other insurance securities and from the standpoint of a valuation upon the usually accepted empirical basis of the proprietary business of the company. Upon both of these bases, the value of the stock would be

nil. Upon consideration of the three bases and in the exercise of their judgment, the committee arrived at a minimum price as of December 31, 1948, of three million dollars.

While from a purely mathematical standpoint, some question may be raised as to the discounting to 1948 of future earnings applicable to the stock at a 10% annual rate, while the interest on the augmentations would be at a much lower rate, still it must be remembered that the determination of price by the committee was not on a mathematical basis, but involved many other considerations. The evidence is uncontradicted that during the period of nearly fourteen years no one has come forth with funds to make these restorations in any manner countenanced by the Rehabilitation Agreement. There is evidence that at times the Stockholders had in mind various plans for making these restorations, but it was pointed out that these arrangements were unsound in that they could not be countenanced by sound insurance accounting practices enforced by state authorities, who regulate the insurance business.

One of the methods suggested was the issuance of notes to non-can policyholders in payment or partial payment of their claims for restoration benefits. Such notes would have to be listed on the balance sheet of an insurer, under recognized insurance accounting practices, as liabilities of the company and thus the surplus of the company would be reduced by the amount of these notes. A financial expert, a member of the Price Determination Committee, gave a great deal of opinion evidence to the effect that securities could not be sold to the public to obtain sufficient funds to make the required restorations. These opinions of this expert have been corroborated to the extent that no one has been able to arrange for the sale of securities during the 13½ years or thereabouts that the opportunity has been present under the terms of the Rehabilitation Agreement. The only evidence that might tend to show that the price

fixed was too low was the offer of American National Insurance Company hereinabove referred to. It is significant that the amount offered for the stock by that company was three million dollars, too. In addition, the offer promised full restoration within seven years, which is, in legal contemplation, a better offer than the promise contained in the Rehabilitation Agreement to make the restorations out of profits or by the other methods therein contemplated, inasmuch as one is a definite promise as to time of performance and the other is indefinite and subject to the contingencies. However, as was pointed out above, this offer was one that could not be entertained under the terms of the Rehabilitation Agreement.

It should be remembered that the plan provides for augmentation of the purchase price in the event that the New Company is sufficiently prosperous to complete restoration prior to the 25-year period from December 31, 1948, and that, in the event restoration cannot be completed by December 31, 1983, the plan will by its own terms fail. These augmentations were incorporated into the plan because the determination of the time of restoration would depend upon the degree of future success enjoyed by the New Company, which cannot be forecast with accuracy. Therefore, the three million dollar figure was set up as a minimum price. If the company proves quite prosperous, the Old Company will participate in this prosperity to some extent. Arrangements of this kind are quite common in the business world. Leases, for instance, are frequently entered into which state a fixed minimum rental, to be augmented by a percentage of the lessee's gross receipts if the percentage exceeds the minimum. Thus, the lessee participates to a certain extent in the future worth of the premises, if the future proves they become more valuable. Other business examples are not hard to find. The plan of augmentation is sufficiently analogous

to these cases drawn from the business world to make further discussion as to the reasonableness of this arrangement for augmentation unnecessary.

As was said before, it was contended by protestants that mutualization of the New Company benefits no one except the management and that the plan, therefore, should not be approved. This contention is based to a large extent upon the fact that the normal benefits of mutualization, that is, the participation in the profits of the operation of the New Company, would not become available for such a long period of time that many of the present policyholders would be dead.

It is to be understood that in almost every mutualization proceeding a long period of time elapses between the development of a plan for mutualization and its ultimate consummation. This fact was as apparent in 1936 as it is at this time. Nevertheless, the Rehabilitation Agreement, which sets forth the rights of the parties herein involved, plainly contemplates mutualization at any time after July 1, 1946, and likewise contemplates that a plan may be developed for mutualization prior to the completion of the restoration of non-can policies. All of such mutualization proceedings must necessarily be viewed as long term operations and for the general benefit of the policyholders of the company being mutualized, in a broad and over-all sense.

Protestants, particularly the group of non-can policyholders, contended very strongly that the plan could not be found to meet the requirements of Section 11527 because it would freeze the method of restoration of the non-can policies to restoration from profits alone. It was pointed out by them that the non-can policyholders, under the terms of Section 20 of the Rehabilitation Agreement, now have at least a hope that the funds necessary for immediate restoration may be raised by the Old Company.

It cannot be gainsaid that if the plan goes into effect, it will have the effect of freezing the method of restoration

as protestants contend. But the non-can policyholders, by accepting reinsurance in the New Company, agreed to all of the terms of the Rehabilitation Agreement and, as has heretofore been pointed out, the Rehabilitation Agreement grants what is in effect an option on the part of the policyholders of the New Company to mutualize. The non-can group cannot now be heard to complain that the effect of the carrying out of this option may freeze the method of restoration to restoration from profits. They made their bargain and as is the case with the Old Company, they cannot now complain of the carrying out of that bargain simply because they do not like it.

It was earnestly contended by the Shareholders that if the plan is approved and adopted, the Insurance Commissioner loses control over restoration. In this regard, it was said that some of the functions that belong to the Insurance Commissioner would be delegated to the voting trustees under the terms of the plan. The answer to this is that the plan does no such thing. The plan cannot and does not amend the Rehabilitation Agreement. As has been noted above, restoration is still a paramount obligation of the New Company and it is the duty of the Commissioner under that agreement to see that restoration is completed with dispatch.

It was also stated that since the voting trustees under the plan were enjoined to see that the company maintained a balance of writings in the Participating and Non-Participating Departments, that this was another delegation of power that belonged to the Commissioner. The answer to this is that although the voting trustees are required to see that such a balance is maintained, a provision of the Rehabilitation Agreement makes the same requirement. The Commissioner still retains full power to enforce all terms of the Rehabilitation Agreement by requiring restorations to be made.

It was contended by the Shareholders that the committee was prejudiced, because it felt that non-can policyholders had made an unconscionable bargain in obtaining their non-can policies in the first place, because the premiums were grossly disproportionate to the benefits granted. There is some evidence that at least one of the members of that committee did feel that such policyholders had made an unusually good bargain, but since the plan did not alter the rights of the non-can policyholders with respect to restoration, that view is of no consequence. There was no evidence that the committee in determining the price of the stock was influenced by the fact that non-can policyholders had made unusually good bargains in purchasing their insurance. It was rceognized by the committee that the contracts must be carried out regardless of the nature of the bargains.

FINDINGS

IT IS HEREBY FOUND AS A FACT that the rights and interests of the New Company, its policyholders, and the holder of its shares are protected under the terms of the plan hereinabove referred to, and that the plan will be fair and equitable in its operation.

CONCLUSIONS OF LAW

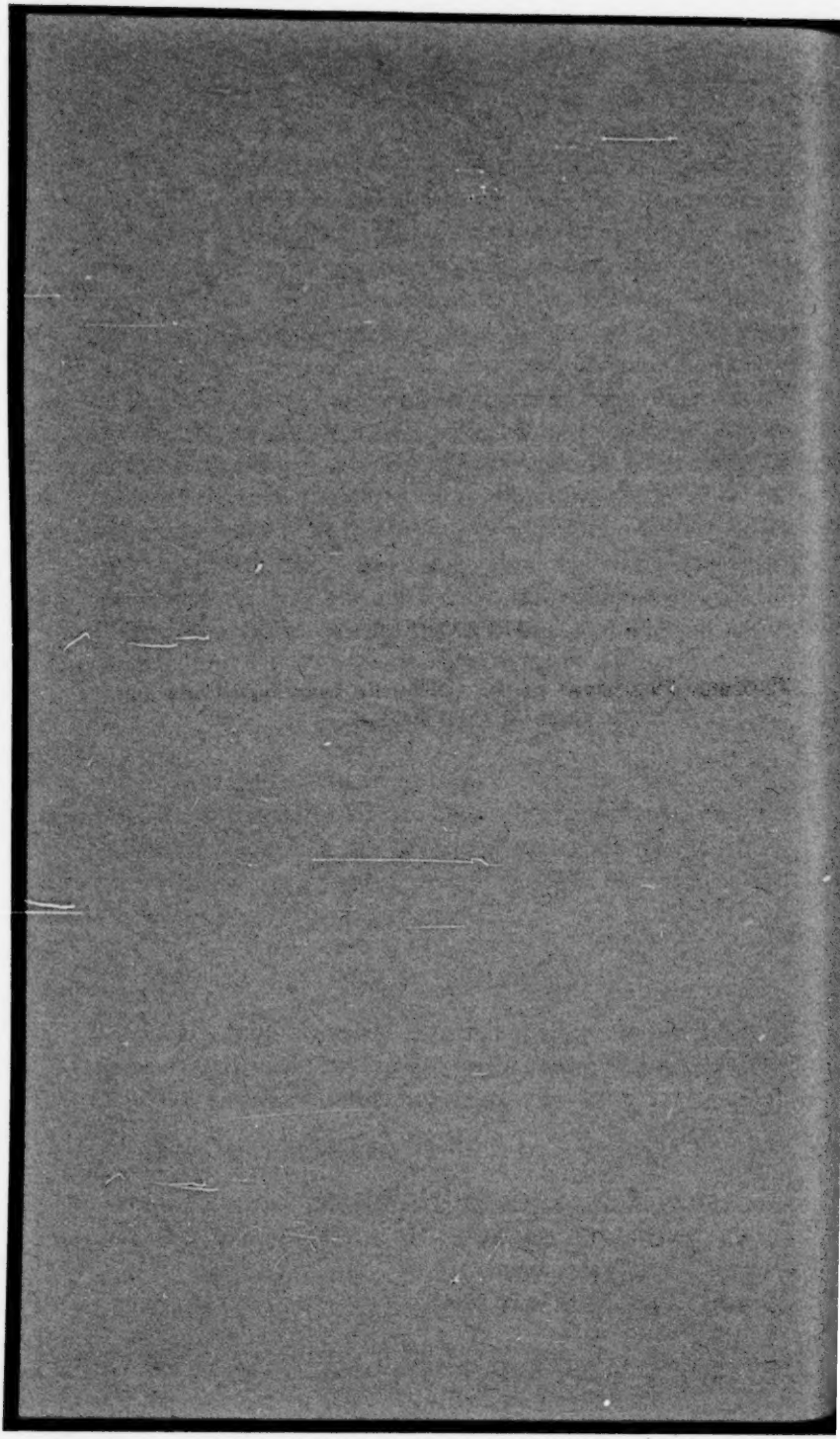
IT IS HEREBY CONCLUDED that the plan is lawful in all respects and meets all requirements of the Insurance Code. The plan is therefore hereby approved.

Dated at Los Angeles, California, September 22, 1950.

WALLACE K. DOWNEY
Wallace K. Downey
Insurance Commissioner
of the State of California.

APPENDIX E

Pertinent Provisions of the California Insurance Code and Code of Civil Procedure



APPENDIX E

Pertinent Provisions of the California Insurance Code and Code of Civil Procedure

CALIFORNIA INSURANCE CODE

(a) Involuntary Mutualization Provisions.

Sec. 1043. Mutualization, reinsurance and rehabilitation.

[*Authority of commissioner: Serving as officer or director in company formed of assets or funds.*] In any proceeding under this article, the commissioner, as conservator or as liquidator, may, subject to the approval of said court, and subject to such liens as may be necessary, mutualize or reinsure the business of such person, or enter into rehabilitation agreements. No commissioner who acts as conservator of such person or who mutualizes, merges or reinsures the business of such person or who enters into rehabilitation agreements affecting such person, and no deputy commissioner who has participated in the administration of the affairs of such person for the commissioner as conservator shall for a period of two years from and after the effective date of such mutualization, reinsurance or rehabilitation become an officer or director of, or serve as an officer or director of, or serve in any position of gain or profit in, any company formed in whole or in part of the assets or funds, or any part of the assets or funds of such mutualized, merged, reinsured or rehabilitated person.

[*Violation of provision: Punishment.*] Every person violating this provision is guilty of a public offense and shall be punished by imprisonment in the State prison not exceeding five years, or in the county jail not exceeding two years, or by a fine not exceeding five thousand dollars ($5,000), or by both such fine and imprisonment.

[*Provision against investment or reinvestment without commissioner's approval.*] Such rehabilitation or reinsurance agreements shall provide that, subsequent to the date thereof and for such period of time as the commissioner may determine, no investment or reinvestment of the assets of the person rehabilitated or reinsured shall be made without first obtaining the written approval of the commissioner.

[*Directing or assisting in investment or reinvestment without, or making in nonconformity with, commissioner's approval: Punishment.*] Every party to such agreement, and every director, officer, agent and employee of such person, and every other person who knowingly in violation thereof directs or aids or assists in causing to be made an investment or reinvestment of any of said assets without first having obtained the written approval of the commissioner, or who makes such investment or reinvestment in nonconformity with the written approval of the commissioner then in effect authorizing such investment or reinvestment, is guilty of a public offense and shall be punished by imprisonment in the State prison not exceeding five years or in the county jail not exceeding two years, or by a fine not exceeding five thousand dollars ($5,000), or by both such fine and imprisonment.

Sec. 1045. Mutualization of life insurer issuing nonassessable policies on a reserve basis: Formation of plan. If at any time after the issuance of an order under section 1011 affecting a life insurer issuing nonassessable policies on a reserve basis and organized with a capital stock evidenced by shares thereof it shall appear to the commissioner that the purposes of section 1011 can be best attained by the mutualization of such life insurer, the commissioner may formulate a plan for the mutualization of such insurer.

Sec. 1046. Same: Mutualization plan: Required provisions. Said mutualization plan shall include provisions for:

(a) [*Acquisition of capital stock.*] The acquisition by such insurer of all outstanding shares of its capital stock at a price and upon terms and conditions to be fixed as hereinafter provided.

(b) [*Retirement of capital stock.*] The retirement of said shares of stock when acquired by such insurer.

(c) [*Amendment of charter.*] The amendment of the charter of such insurer so as to enable it to transact its business as a mutual insurer issuing nonassessable policies on a reserve basis.

(d) [*Payment of claims.*] The manner in which and the time within which, after mutualization is effected, matured and maturing claims against such insurer shall be paid to the lawful holders thereof.

(e) [*Submission of plan to policyholders.*] The submission of said mutualization plan to the policyholders of such insurer under such procedure as shall be set forth in the plan or prescribed by said court, for their approval or rejection.

(f) [*Notice to shareholders.*] Notice to the shareholders of such insurer, in such manner and at such time after the approval of said mutualization plan by said policyholders, as the court may direct.

Sec. 1047. Same: Optional provisions. Said mutualization plan may include provisions:

(a) [*Imposing moratorium against provisions calling for making loans, etc.*] Imposing a moratorium against the provisions of the life insurance policies issued by such

insurer and then in force calling for the making of loans on the security of such policies and for the payment of money upon the surrender of such policies, for a period and to an extent to be named in such provisions imposing such moratorium, and subject to extension, change or prior termination only upon the written approval of the commissioner.

(b) [*Imposing liens, etc.*] Imposing liens upon, or otherwise adjusting, the policies of the insurer so as to create or make available the minimum paid-in capital required of such an insurer to be admitted and such additional paid-in capital as will be reasonably sufficient to enable such insurer to carry on its business.

No lien or adjustment of such insurer's policies shall be made or imposed which has the effect of creating or making available for distribution to the shareholders of such insurer assets otherwise unavailable therefor.

(c) [*Regulating and adjusting rights of holders of policies of different classes, etc.*] Regulating and adjusting the respective rights of holders of policies of different classes to participate in the profits or savings which may be made by such insurer when mutualized.

(d) [*Regulating compensation of shareholders for interest other than goodwill.*] Regulating the manner in which and the time at which the shareholders of such insurer shall be compensated for their proprietary interest, then existing, in the assets of such insurer other than goodwill.

(e) [*Regulating compensation of shareholders for interest in goodwill.*] Regulating the manner in which the shareholders of such insurer shall be compensated for their proprietary interest in the goodwill, if then existing, of such insurer; provided, however, that no shareholder shall be compensated for his proprietary interest in such goodwill

while any moratorium imposed under subdivision (a) of this section is in effect, nor while any lien imposed under subdivision (b) of this section exists, nor until all other indebtedness of such insurer existing at the time of mutualization has been fully paid and discharged or full provision made for its payment, nor otherwise than out of surplus earnings.

(f) [*Regulating other matters.*] Regulating such other matters as may, in the opinion of the commissioner, require regulation in the interest of expediency or otherwise.

Sec. 1048. Same: Application for order to submit plan: Issuance of order. Upon formulation of said mutualization plan the commissioner shall submit the same to said court with his application for an order of said court directing the commissioner to submit said mutualization plan to the persons named in subdivision (e) of section 1046, under such procedure as shall be set forth in the plan or prescribed by said court, for their approval or rejection, and the court shall issue such order.

Sec. 1049. Same: Policyholder entitled to one vote: When plan deemed approved or rejected: Certification of rejection. Each policyholder of such insurer shall be entitled to one vote, regardless of the amount for which, or the number of policies under which, he is insured. Such mutualization plan shall be deemed approved by the said policyholders if a majority of the policyholders voting for and against it shall have approved it, and shall be deemed rejected if a majority of the policyholders voting for and against it shall have rejected it. In the event that said plan of mutualization is rejected by the policyholders of such insurer, the commissioner shall certify the fact of such rejection to said court, whereupon he may proceed further as hereinbefore provided in this article.

Sec. 1050. Same: Certification of approval of plan: Order directing giving notice of approval: Petition by shareholder disapproving plan: Petition for appointment of appraisers. In the event that said plan of mutualization is approved by said policy holders, the commissioner shall certify to the said court the fact of such approval and the number of votes cast for and against such mutualization plan. Said court shall thereupon issue its order directing the commissioner to give notice, as provided in said mutualization plan or as the court may otherwise prescribe, to the shareholders of such insurer of the approval of said mutualization plan by said policyholders. Said order shall direct the commissioner to transmit to each such shareholder by mail addressed to his address as it appears upon the records of such insurer, a true copy of said order and of said mutualization plan approved by said policyholders, and shall fix a time, not less than thirty nor more than sixty days from the date of such order, within which any such shareholder may file with said court a petition for the disapproval of said mutualization plan or for its modification in such manner, as shall be set forth in such petition, and within which any such shareholder and the commissioner may file with said court a petition for the appointment of one or more appraisers to appraise the value of the then outstanding shares of capital stock of such insurer.

Sec. 1051. Same: Notice of hearings of petitions: Precedence of petitions: Approval or disapproval of plan: Appointment of apparisers: Appraisement. After the expiration of the time fixed in the order provided for in section 1050, and upon the filing of such petition, said court shall direct notice of hearing of said petitions to be given to the commissioner and to such petitioners as are shareholders of such insurer. At such hearing, all petitions for the disapproval and all petitions for the modification of said mutualization plan shall be given precedence over all

petitions for the appointment of one or more appraisers. Upon hearing of all such petitons for the disapproval and for the modification of said mutualization plan, said court shall either approve said mutualization plan or disapprove it or modify it in such manner and to such extent, not inconsistent with the provisions of this article, as to said court shall seem appropriate. In the event of the disapproval of said mutualization plan the court shall deny all petitions for the appointment of one or more appraisers. In the event of the approval or modification of said mutualization plan, the court shall, upon hearing of the petitions for the appointment of appraisers, appoint one or more appraisers, who shall appraise the then outstanding shares of the capital stock of such insurer, without regard to any appreciation or depreciation arising out of said mutualization plan as so approved or modified. Such appraisement shall fix the reasonable value of such shares of capital stock, including the goodwill, if any, of such insurer, and shall state the value, if any, assigned to such goodwill; and if the appraisers shall have found that such insurer has no goodwill, such finding shall be stated. Such appraisement, when confirmed by said court, shall be final and conclusive.

Sec. 1052. Same: Completion of mutualization. Thereupon the commissioner shall:

(a) [*Payment to shareholders.*] Pay to each of such shareholders or his assignee or nominee, upon surrender of the shares held by such shareholder, the value of said shares so ascertained; subject, however, to the restrictions of subdivisions (d) and (e) of section 1047, and subject, also to the terms and conditions of the mutualization plan as approved or modified.

(b) [*Appointment of directors.*] Appoint, with the approval of the court, the requisite number of directors in whom shall thereafter be vested the control and manage-

ment of the assets and business of such insurer until their successors shall have been elected and qualified.

(c) [*Transference of property, etc., to proper officers.*] Transfer, upon the order of said court, to the appropriate officers appointed by such directors, the property, real and personal, and the books, records, accounts and papers of such insurer; provided, however, that the commissioner may retain, as a deposit, so much of such property as he deems necessary to defray additional costs and expenses incurred or to be incurred in connection with any proceeding under this article affecting such property or business.

Sec. 1053. Same: Cessation of office by directors in office: Termination of voting rights of shareholders: Status of mutualized insurer: Power to issue nonassessable policies. Immediately upon the appointment of the directors as provided in subdivision (b) of section 1052, the directors theretofore holding office shall cease to hold office, and all rights of the shareholders of such insurer to vote at any meeting of such insurer shall absolutely cease and such shareholders shall retain only such interest in such corporation or in the property or assets thereof as shall be provided in said mutualization plan, and such insurer shall thereupon be and become a mutual life insurer under such corporate name as may have been set forth in its charter, as amended, to be conducted not for profit, but solely for the mutual benefit, ratably, of all its policyholders, and shall, upon issuance to it by the commissioner of a certificate of authority, have power to issue nonassessable policies on a reserve basis subject to all provisions of law applicable to incorporated life insurers issuing nonassessable policies on a reserve basis, but shall be exempt from the provisions of Chapter 7, Part 2, Division 2 of this code.

Sec. 1054. Same: Effect of mutualization upon existing suits, contracts and rights: Rights, powers and duties of mutualized insurer. Such insurer, after mutualization, shall be a continuation of the original insurer, and such mutualization shall not affect existing suits, rights or contracts except as provided in said mutualization plan as approved. Such insurer, after mutualization, shall exercise all the rights and powers and perform all the duties conferred or imposed by law upon insurers writing the classes of insurance written by it, and to protect rights and contracts existing prior to mutualization, subject to the effect of said mutualization plan.

Sec. 1055. Same: Powers and duties of commissioner as to mutualized insurers: Issuance of certificate of authority. The commissioner shall exercise the powers and discharge the duties, concerning any insurer so mutualized, that are applicable to domestic insurers issuing policies of the same class. He shall issue a certificate of authority to transact the proper classes of insurance in this State to any insurer so mutualized which is solvent under Article 13, Chapter 1, Part 2, Division 1 of this code and which has fully complied with the laws of this State.

Sec. 1056. Same: Payments of costs and expenses. All costs and expenses connected with proceedings for the mutualization of such insurer shall be paid by the commissioner out of the funds of such insurer, whether or not mutualized, subject to the approval of said court.

(b) Voluntary Mutualization Provisions.

Sec. 11525. Authorization to mutualize. A solvent domestic incorporated insurer having a paid-in capital represented by outstanding shares of capital stock and issuing,

on a reserve basis, nonassessable policies of life insurance or of both life and disability insurance, may convert itself into an incorporated mutual life insurer, or life and disability insurer, issuing nonassessable policies on a reserve basis. To that end it may provide and carry out a plan for the acquisition of the outstanding shares of its capital stock for the benefit of its policyholders, or any class or classes of its policyholders, by complying with the requirements of this chapter.

Sec. 11526. Method of mutualization. Such plan shall include appropriate proceedings for amending the insurers articles of incorporation to give effect to the acquisition, by said insurer, for the benefit of its policyholders or any class or classes thereof, of the outstanding shares of its capital stock and the conversion of the insurer from a stock corporation into a nonstock corporation for the benefit of its members. The members of such nonstock corporation shall be the policyholders from time to time of the class or classes for whose benefit the stock of the insurer was acquired, and no other persons. Such plan shall be:

(a) Adopted by a vote of a majority of the directors.

(b) Approved by the vote of the holders of at least a majority of the outstanding shares at a special meeting of shareholders called for that purpose, or by the written consent of such shareholders.

(c) Submitted to the commissioner and approved by him in writing.

(d) Approved by a majority vote of all the policyholders of the class or classes for whose benefit the stock is to be acquired voting at an election by the policyholders called for that purpose, subject to the provisions of Section 11528. The terms "policyholder" and "policyholders" as used in this chapter shall be deemed to mean the person or

persons insured under an individual policy of life insurance, or of disability insurance, or of any combination of life and disability insurance. They shall also include the person or persons to whom any annuity or pure endowment is presently or prospectively payable by the terms of an individual annuity or pure endowment contract, except where the policy or contract declares some other person to be the owner or holder thereof, in which case such other person shall be deemed the policyholder. In any case where such policy or contract names two or more persons as joint insureds, payees, owners or holders thereof, the persons so named shall be deemed collectively to be but one policyholder for the purpose of this chapter. In any case where a policy or contract shall have been assigned by assignment absolute on its face to an assignee other than the insurer, and such assignment shall have been filed at the principal office of the insurer at least 30 days prior to the date of any election or meeting referred to in this chapter, then such assignee shall be deemed at such election or meeting to be the policyholder. For the purpose of this chapter the terms "policyholder" and "policyholders" include the employer to whom, or a president, secretary, or other executive officer of any corporation or association to which a master group policy has been issued, but exclude the holders of certificates or policies issued under or in connection with a master group policy. Beneficiaries under unmatured contracts shall not as such be deemed to be policyholders.

(e) Filed in the office of the Insurance Commissioner after having been approved as provided in subdivisions (b), (c) and (d) of this section.

Sec. 11527. Examination of plan by commissioner: Conditions prerequisite to approval. The commissioner shall examine the plan submitted to him under the provisions of subdivision (c) of section 11526. He shall not

approve such plan unless in his opinion the rights and interests of the insurer, its policyholders and shareholders are protected nor unless he is satisfied that the plan will be fair and equitable in its operation.

CALIFORNIA CODE OF CIVIL PROCEDURE

Sec. 1094.5. [Inquiry into validity of administrative order or decision.] (a) Where the writ is issued for the purpose of inquiring into the validity of any final administrative order or decision made as the result of a proceeding in which by law a hearing is required to be given, evidence is required to be taken and discretion in the determination of facts is vested in the inferior tribunal, corporation, board or officer, the case shall be heard by the court sitting without a jury. All or part of the record of the proceedings before the inferior tribunal, corporation, board or officer may be filed with the petition, may be filed with respondent's points and authorities or may be ordered to be filed by the court. If the expense of preparing all or any part of the record has been borne by the prevailing party, such expense shall be taxable as costs.

(b) The inquiry in such a case shall extend to the questions whether the respondent has proceeded without, or in excess of jurisdiction; whether there was a fair trial; and whether there was any prejudical abuse of discretion. Abuse of discretion is established if the respondent has not proceeded in the manner required by law, the order or decision is not supported by the findings, or the findings are not supported by the evidence.

(c) Where it is claimed that the findings are not supported by the evidence, in cases in which the court is authorized by law to exercise its independent judgment on the evidence, abuse of discretion is established if the court determines that the findings are not supported by the weight

of the evidence; and in all other cases abuse of discretion is established if the court determines that the findings are not supported by substantial evidence in the light of the whole record.

(d) Where the court finds that there is relevant evidence which, in the exercise of reasonable diligence, could not have been produced or which was improperly excluded at the hearing before respondent, it may enter judgment as provided in subdivision (e) of this section remanding the case to be reconsidered in the light of such evidence; or, in cases in which the court is authorized by law to exercise its independent judgment on the evidence, the court may admit such evidence at the hearing on the writ without remanding the case.

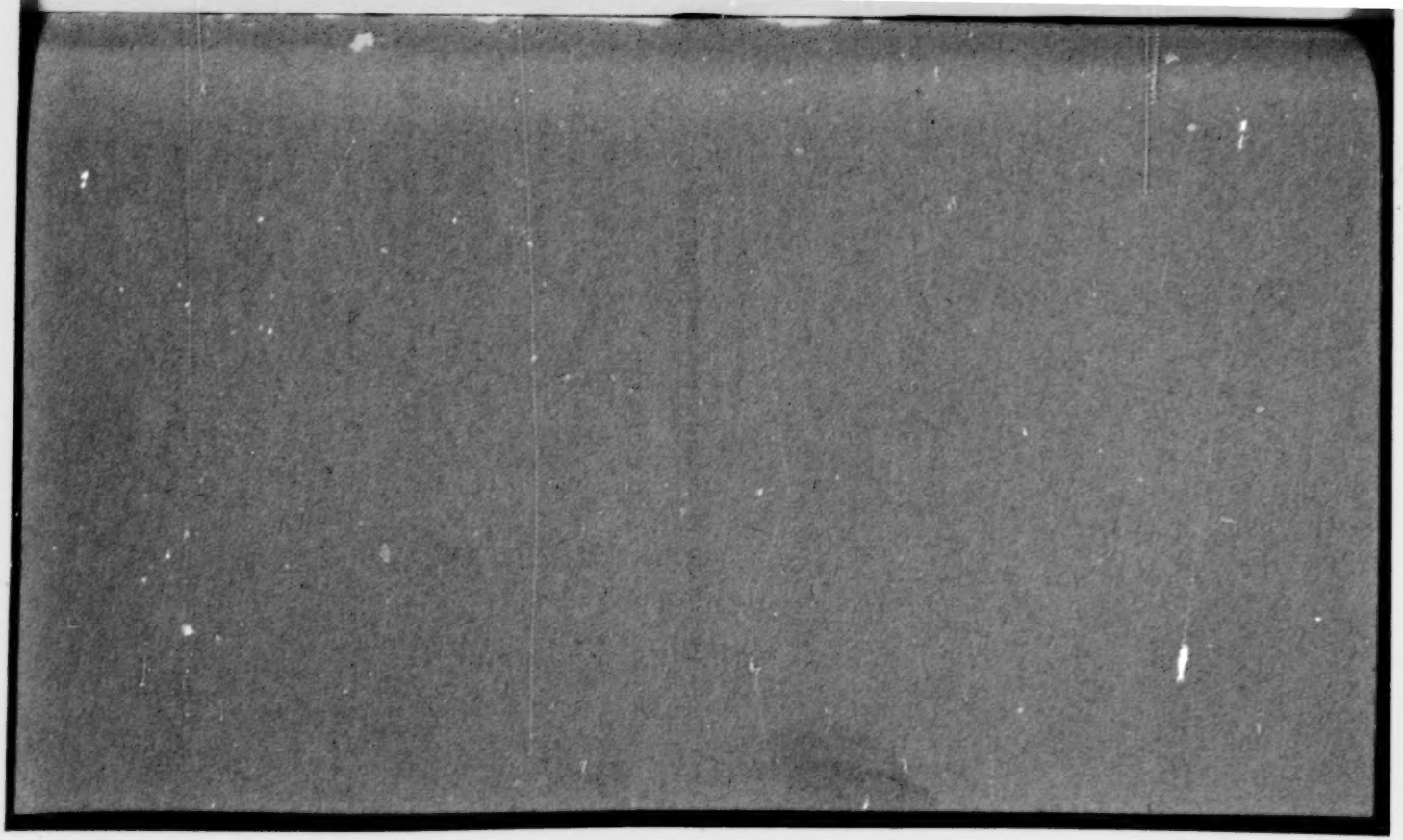
(e) The court shall enter judgment either commanding respondent to set aside the order or decision, or denying the writ. Where the judgment commands that the order or decision be set aside, it may order the reconsideration of the case in the light of the court's opinion and judgment and may order respondent to take such further action as is specially enjoined upon it by law but the judgment shall not limit or control in in [sic] any way the discretion legally vested in the respondent.

(f) The court in which proceedings under this section are instituted may stay the operation of the administrative order or decision pending the judgment of the court, or until the filing of a notice of appeal from the judgment or until the expiration of the time for filing such notice whichever occurs first; provided that no such stay shall be imposed or continued if the court is satisfied that it is against the public interest. If an appeal is taken from a denial of the writ, the order or decision of the agency shall not be stayed except upon the order of the court to which such appeal is taken; provided that, in cases where a stay is in effect

at the time of filing the notice of appeal, such stay shall be continued by operation of law for a period of twenty (20) days from the filing of such notice. If an appeal is taken from the granting of the writ, the order or decision of the agency is stayed pending the determination of the appeal unless the court to which such appeal is taken shall otherwise order. Where any final administrative order or decision is the subject of proceedings under this section, if the petition shall have been filed while the penalty imposed is in full force and effect the determination shall not be considered to have become moot in cases where the penalty imposed by the administrative agency has been completed or complied with during the pendency of such proceedings.

APPENDIX F

Rehabilitation and Reinsurance Agreement



APPENDIX F

Rehabilitation and Reinsurance Agreement

This Agreement, made and entered into as of the 22nd day of July, 1936, between Pacific Mutual Life Insurance Company, a California corporation, and Samuel L. Carpenter, Jr., Insurance Commissioner of the State of California, as conservator of The Pacific Mutual Life Insurance Company of California, a California corporation,

Witnesseth:

That for and in consideration of the covenants and agreements hereinafter contained, the parties hereto agree as follows:

Definitions

(1) "Commissioner" shall mean Samuel L. Carpenter, Jr., in his capacity as Insurance Commissioner of the State of California, or his successors in office as such Commissioner.

"Conservator" shall mean Samuel L. Carpenter, Jr., Insurance Commissioner of the State of California, in his capacity as Conservator of The Pacific Mutual Life Insurance Company of California, or his successors in office as such Conservator.

"Old Company" shall mean The Pacific Mutual Life Insurance Company of California. "New Company" shall mean Pacific Mutual Life Insurance Company.

"The Court" shall mean the Superior Court of the State of California, in and for the County of Los Angeles.

"Non-Can Policies" shall mean those policies of the Old Company usually known as its "Non-Cancellable Income Policies" including the Aggregate form thereof.

"States" when referred to a governmental subdivision shall be deemed to include Territories and the District of Columbia.

"Properties of the Old Company" shall mean all books, records, property, real and personal, tangible and intangible, and all other assets of every kind, character, and description whatsoever, and wheresoever situated, owned by the Old Company at the time of the appointment of the Conservator which shall not have been applied by him against his subscription for stock of the New Company or disposed of by him in the due course of his administration as Conservator, plus all property acquired by the Conservator, and the income therefrom collected by him, except (a) the stock of the New Company held by him, and (b) rights or claims, if any of whatsoever nature which the Old Company may have against any of the present or past officers, directors, or employees, as such, of the Old Company, or against any other person, firm, or corporation, by reason of or in connection with wrongful or illegal acts or omissions, if any, of any of the past or present officers, directors, or employees of the Old Company, including rights or claims on any fidelity or surety bond or bonds given to or in favor of the Old Company to secure the faithful performance by any of its officers, directors, or employees of any of their duties as such.

"Effective Date of this Agreement" shall mean July 22, 1936, at the hour of one o'clock P. M. Pacific Standard Time.

"Liquidator" shall mean any person hereafter appointed Liquidator of the Old Company in the proceeding now pending in the Court entitled "Samuel L. Carpenter, Jr., Insurance Commissioner of the State of California vs. The Pacific Mutual Life Insurance Company of California", and bearing number 404673 in the records of the Court; and any person succeeding to the office of such Liquidator.

Transfer of Assets

(2) The Conservator agrees, by appropriate instrument of conveyance, to sell, assign, convey, release, transfer, set over, and deliver, to the New Company, the properties of the Old Company; and to execute any and all further documents or instruments as may be reasonably necessary to effectuate and confirm the title of the New Company thereto.

The Conservator shall not be required to make manual delivery of any cash or securities deposited by the Old Company with any governmental authority as a condition to the conduct of its business, nor to make manual delivery of any premiums or other assets which are in the possession of receivers of the Old Company or its assets or business, or in the possession of other governmental authorities, in states other than California; but in connection with receivership or other proceedings in such other states, the Conservator shall do any and all things proper for him to do to bring about and accomplish the delivery and transfer of such premiums or other assets to the New Company.

The Conservator shall transfer and deliver to the New Company the full amount of all premiums on any policy reinsured and assumed hereunder which have been paid to the Conservator on or after the effective date of the agreement, and the New Company shall credit the holder of such policy with the payment of such premiums accordingly, subject to repayment as hereinafter provided in the event the holder of such policy shall elect not to accept such reinsurance and assumption by the New Company. If any policy holder of the Old Company whose policy may be reinsured or assumed hereunder shall have paid his premium thereon to the Conservator subsequent to the effective date of this agreement and shall thereafter elect to reject reinsurance and assumption of his such policy hereunder:

and if the Court shall direct the Conservator or Liquidator to return said premium (or the net premium or premiums less charge for insurance service or collection charge or otherwise): then and in those events the New Company shall repay to the Conservator or Liquidator, on demand, said premium, or so much thereof as the Court may have ordered returned by the Conservator or Liquidator, as aforesaid. Pursuant to the provisions of Section 1043 of the Insurance Code of the State of California it is agreed that subsequent to the effective date of this agreement, and for such period of time as the Commissioner may determine, no investment or reinvestment of the assets of the Old Company shall be made without first obtaining the written approval of the Commissioner.

Reinsurance and Assumption of Policies
Other Than Non-Can Policies

(3) The New Company does hereby reinsure and assume, as of the effective date of this agreement, with the exception hereinafter provided, the liability of the Old Company and of the Conservator under all life, endowment, annuity and term policies and contracts of insurance, and all other policies and contracts of insurance, including, without limiting the same to, health and accident benefits, waiver of premium disability benefits, permanent and total disability benefits, home office employees disability benefit plan, and all supplementary contracts, annuity contracts, and all reinsurance contracts, issued or assumed by the Old Company and outstanding and in force on the books and records of the Old Company at the effective date of this agreement, or issued by the Conservator in his name as Conservator, in the name of the Old Company, or in the name of the New Company, subject, however, to any and all defenses, offsets, counterclaims, cross-complaints, and

rescission rights against said policies or contracts or against any claims and actions thereon, which would have been available to the Old Company or the Conservator as aforesaid had this agreement not been made; provided, however, that no outstanding Non-Can Policies are reinsured or assumed under this paragraph, and all of such policies are hereby expressly excepted from the obligations of the New Company under this paragraph.

Reinstatement of Lapsed Policies

(4) The New Company will reinstate any policies heretofore issued, assumed, or reinsured by the Old Company, which are not excepted from the obligations of the New Company contained in the foregoing paragraph and which at the effective date of this agreement, by their terms, were entitled to reinstatement, provided that all requirements necessary to procure a reinstatement of said policies under their terms are fulfilled to the satisfaction of the New Company.

The New Company will also reinstate, during the lifetime of the insured and provided the insured is not in such condition as to be eligible for benefits under the policy, without evidence of insurability, any of the policies reinsured and assumed under Paragraph (3) hereof, which have lapsed since the effective date of this agreement, upon written application therefor by the insured and the payment of all premiums in arrears, if such application is made and premiums are paid within seventy five (75) days after the entry of the order of the Court approving this agreement. Upon the reinstatement of such lapsed policy it shall, for all purposes, be treated (but only from and after the date of reinstatement) the same as if it had been in force on the effective date of this agreement and be subject to the terms and conditions of this agreement.

Payment of Policy Claims Other Than Claims on Non-Can Policies

(5) The New Company will pay in full, in accordance with the terms and conditions of all policies including annuities under which claims shall have been or may be made, and whether or not the claims arose or matured prior or subsequent to the effective date of this agreement, all policy claims against the Old Company (except claims on Non-Can Policies) including, without limiting the same to, claims for death benefits, matured endowments, annuity payments, permanent total disability and premium waiver benefits, accident and sickness benefits, payments under policy settlement agreements, policy dividends let at interest with the Old Company prior to the effective date of this agreement, and payments under all other matured contracts under which the proceeds of policies and contracts were left with the Old Company prior to the effective date of this agreement; and the New Company will assume the liabilities of the Old Company with respect to deposits, moneys left with the Old Company at interest, overpayments, duplicate payments or advance payments of premiums, and return of premiums arising from cancellations prior to July 22, 1936; all subject, however, to any and all defenses, offsets, counter-claims, cross-complaints, and rescission rights against any such claim or claims which would have been available to the Old Company had this agreement not been made.

Participating Department

(6) The New Company agrees to establish a separate department for Participating Life Insurance, and to allocate thereto specifically or in tenancy in common that portion of the assets conveyed to it by the Conservator (other than the Three Million Dollars ($3,000,000.) transferred to the

New Company for its capital stock) in the ratio in which assets appearing on the books of the Life Department of the Old Company were credited to the Participating Life Department of the Old Company on its books as of July 22, 1936, subject to such changes as may have been made therein in the ordinary course of the operations of the business of the Old Company by the Conservator, including the writing of the new participating life insurance by the New Company, and except assets of the book value of One Million, Seven Hundred Ninety-Two Thousand, One Hundred Eighteen Dollars and Ninety-seven Cents ($1,792,118.97) transferred by the Conservator to the Accident and Health Department.

The said Three Million Dollars ($3,000,000.) transferred to the New Company for its capital stock constitutes and shall constitute the capital and paid-in surplus of the New Company; and neither the Participating Department nor the holders, present or future, of participating policies shall have any right, claim, or interest therein prior to other Departments or their policy holders. The said assets transferred to the Accident and Health Department are and shall be the property of the said Department free from any claim of the Participating Department, or the holders, present or future, of participating policies.

It is hereby agreed by the New Company, and all persons accepting reinsurance hereunder do by such acceptance agree that the assets of the Participating Department, and its business, and the receipts in respect of said business shall, subject to the limitations hereinafter contained, be appropriated and held as absolutely for the benefit of and to the security of the policies and policy holders of that Department as though they belonged to a mutual insurance company carrying on no other business; and, to the extent of the reserves from time to time required on the policies and policy liabilities of said Department, in priority to the claims

of all other creditors, past, present, and future, of said Department.

The Board of Directors of the New Company shall, from time to time, and at least annually, transfer from the Participating Department to the funds of the New Company available for its general corporate purposes, such sums as it may deem available, if any, but in no event exceeding in the aggregate ten percent. (10%) of the net profits (before dividends, and without charging thereto cost of acquisition of new business) then accrued on policies of the Old Company reinsured hereunder earned subsequent to the effective date of this agreement (whether arising from mortality savings, investment income, expense savings, or otherwise, and after taking into consideration gains or losses on the sale or other disposition of assets, and such reasonable adjustment in the value of any assets, or reserves for anticipated losses thereon, or otherwise, as the Board of Directors of the New Company may from time to time establish, subject only to readjustment upon the order of the Commissioner made in the course of or as a result of any examination of the New Company). Any portions of such ten percent. (10%) not so transferred at any time shall be cumulative, and shall be transferred from time to time thereafter, from profits, and subject to limitations as aforesaid. Any statute of limitations which might apply to bar the right to require such transfer is hereby waived.

Any surplus from time to time existing in said Department (whether arising from mortality savings, investment income, expense savings, or otherwise, and after taking into consideration gains or losses on the sale or other disposition of assets, and such reasonable adjustments in the value of any assets, or reserves for anticipated losses thereon, or otherwise, as the Board of Directors of the New Company may from time to time establish, subject only to readjustment upon the order of the Commissioner made in

the course of or as a result of any examination of the New Company), may be used only for the following purposes:

(a) The payment of policy dividends to policy holders in accordance with the terms of their policies and in such amounts as the Board of Directors of the New Company may from time to time consider proper and advisable, taking into consideration the amount of earnings and other relevant data.

(b) For the payment of any of the costs and expenses of operation of said Department, including the acquisition and carrying of new business written by said Department in such amounts as the Board of Directors of the New Company may from time to time deem reasonably necessary or desirable.

(c) Necessary working capital may be supplied to said Department from time to time from any moneys available for general corporate purposes; and the Board of Directors of the New Company shall, when in their discretion it shall appear practicable, in subordination to the rights of the policy holders of said Department, and from surpluses accumulated in said Department after the payment of reasonable and appropriate dividends to the policy holders thereof, as provided in sub-paragraph (a) of this paragraph 6, restore the amount of the working capital so supplied, together with interest thereon at the average rate of interest earned by the New Company during the period, to the sources from which it came.

(d) For the payment into funds of the New Company available for its general corporate purposes of a portion not exceeding ten percent. (10%) of the net earnings of the participating policies of the Old Company reinsured hereunder, as hereinbefore provided. In computing dividends payable to participating policy holders, any amounts paid under this subparagraph shall be charged against said

policies reinsured and no part thereof shall be charged against participating policies issued by the New Company.

(e) Any remaining portion of said surplus shall be kept separate and distinct from the funds of all other departments; and shall be held as absolutely for the security of and the benefit of the policy holders of the Participating Department as though it belonged to a mutual company carrying on no other business.

Non-Participating Department

(7) The New Company further agrees to establish a separate department for its Non-Participating Life Insurance, and to allocate thereto specifically or in tenancy in common that portion of the assets conveyed to it by the Conservator in the ratio in which assets appearing on the books of the Life Department were credited to the Non-Participating Department of the Old Company on its books as of July 22, 1936, subject to such changes as may have been made therein in the ordinary course of the operation of the business of the Old Company by the Conservator, including the writing of new non-participating life insurance by the New Company.

It is hereby agreed by the New Company and all persons accepting reinsurance hereunder do by such acceptance agree that the assets from time to time held in said Non-Participating Department shall, to the extent of the reserves from time to time required on the policies and policy liabilities of said Department, be appropriated, and held as absolutely for the benefit of and to the security of the policies and policy holders of said Department as though they belonged to a company carrying on no other business, and in priority to the claims of all other policy holders or creditors, past, present, or future, of the New Company.

Any surplus from time to time existing in said Non-Participating Department (whether arising from mortality

savings, investment income, expense savings, or otherwise, and after taking into consideration gains or losses on the sale or other disposition of assets and such reasonable adjustments in the value of any assets, or reserves for anticipated losses thereon, or otherwise, as the Board of Directors of the New Company may from time to time establish, subject only to readjustment upon the order of the Commissioner made in the course of or as a result of any examination of the New Company) may from time to time be used for the general corporate purposes of the New Company subject to any express limitations herein contained.

Accident and Health Department

(8) The New Company further agrees to establish a separate department for its Accident and Health Insurance (including Non-Can Policies) and to allocate thereto the assets conveyed to it by the Conservator which had been credited to the Accident and Health Department of the Old Company on its books as of July 22, 1936, and those assets of the book value of One Million, Seven Hundred Ninety-two Thousand, One Hundred Eighteen and 97/100 Dollars ($1,792,118.97) heretofore transferred by the Conservator to the Accident and Health Department, subject to such changes as may have been made therein in the ordinary course of the operation of the business of the Old Company by the Conservator, including the writing of new accident and health insurance by the New Company.

It is hereby agreed by the New Company, and all persons accepting reinsurance hereunder do by such acceptance agree, that the assets from time to time held in said Department shall, to the extent of the reserves from time to time required on the policies and policy claim liabilities of said Department, be appropriated for the benefit of and to the security of the policies and policy claim liabilities hereof

Prem. Class	Issued Under Rate Books	Policy Forms	Issued Under Policy Numbers	Percentage of Original Monthly Benefit Assumed By New Company
1918	A1445-A1445Z A1445Y-A1445X A1445W	A231 to A288 Inc.	2658601 to 2698150 4600501 to 4628000 4711101 to 4712000 4730901 to 4731100	20%
1921	A1687-A1687Z A1687Y-A1687X A1687W	A291 to A 294 Inc. A365-A366	4628001 to 4700000	35%
1926	A1958-A1958Z A1958Y	A382-A383 A386-A387 A387Z	5500001 to 5600000	45%
1929	A2293	A382-A383 A386-A387 A387Z	5600001 to 5620000	55%
1931	A2367	A753 to A756 Inc. A763-A764	5620001 to 5635000	65%
1932	A2432-A2432Z A2499	A775 to A780 Inc.	5635001 to 6000000	90%
	A2499	Aggregate A1216 to A1221 Inc.	6500001 to 7000000	90%
1935	A2567	Aggregate A1226 to A1229 Inc.	7000001 to 7100000	90%

NOTE: All of the above mentioned Rate Books are Rate Books issued by the Old Company and copies are on file at the office of the New Company at 523 West Sixth Street, Los Angeles, California, and in the offices of the Insurance Commissioners or similar public officials of each state in which the Old Company has been transacting insurance business, except in states where such filing is not required by law.

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Notwithstanding the foregoing limitation on the obligation of the new Company to make monthly disability payments at such rates on such policies, to be entitled to the reinsurance and assumption of his Non-Can Policy by the New Company as aforesaid, the policy holder shall be obligated to continue to make premium payments as originally provided in his policy.

Reinstatement of Lapsed Non-Can Policies

(12) The provisions of paragraph 4 of this agreement with respect to reinstatement of lapsed policies other than Non-Can Policies shall apply to Non-Can Policies, subject to the terms, conditions and limitations contained in paragraphs 10 and 11 hereof.

Payment of Claims on Non-Can Policies in Respect of Disabilities Existing Prior to Effective Date of this Agreement

(13) The New Company shall be obligated to pay all disability benefits under Non-Can Policies for disabilities commencing prior to the effective date of this agreement with respect to which claims or notices of claims were duly filed in accordance with the terms of such policies and in any event not later than twenty (20) days after the effective date of this agreement, and all payments under settlement agreements made by the Old Company with claimants under such policies without any deduction or limitation whatsoever, but subject to all of the terms and provisions of such Non-Can Policies, and subject to the terms of any such settlements agreements; and subject, further, to any and all defenses, offsets, counterclaims, cross-complaints, and rescission rights against any such claim or claims, which would have been available to the Old Company or to the Conservator as aforesaid had this agreement not been made.

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Restoration of Benefits under Non-Can Policies

(14) The Board of Directors of the New Company shall from time to time transfer from the funds of the New Company available for its general corporate purposes to a special fund for the restoration of benefits under Non-Can Policies in such manner as the Board of Directors with the approval of the Commissioner may from time to time determine, such amounts as said Board of Directors in its discretion shall determine to be not reasonably required for the reasonable, proper and profitable conduct of the operations of the New Company as a going concern. At time of any examination of the New Company by the Commissioner, the Commissioner may require the transfer of additional funds to such special fund, to the extent such additional funds available for general corporate purposes are in his opinion available without interfering with the proper and profitable conduct of the business of the New Company as a going concern.

The moneys and other assets from time to time held in such special fund shall be used by the New Company, with the approval of the Commissioner, and in such manner as he may from time to time require, for the purpose of paying additional disability benefits to holders of Non-Can Policies then thereafter, or theretofore entitled thereto, in excess of the amounts required to be paid under paragraph 11 hereof, to the end that the benefits originally provided in said Non-Can Policies as written may eventually be fully paid, including eventual full payment of benefits becoming due prior to the time of such restoration, with interest on deferred restoration payments of such benefits at the rate of three and one-half percent. (3½%) per annum. The extent and manner of the restoration so required or approved by the Commissioner shall be binding upon all holders of Non-Can Policies, and all other persons interested therein.

The new Company may at any time, with the approval of the Commissioner, transfer all of such special fund to the reserves for Non-Can Policies, and, with the approval of the Commissioner, may fully assume and reinsure all Non-Can Policies hereby partially and conditionally reinsured, to the full amount thereof and in accordance with the terms thereof as written; and if the Commissioner at the time of any examination of the New Company shall determine that in his opinion the amount of such special fund is sufficient to permit the establishment therefrom of adequate reserves for the full reinsurance of such Non-Can Policies, he may require such transfer and full reinsurance.

Upon such full reinsurance with the approval of or in accordance with the requirements of the Commissioner, the benefits on Non-Can Policies shall be deemed fully restored.

After the benefits on Non-Can Policies shall have been fully restored, the said special fund shall be abolished, and any assets remaining therein at that time shall be available for the general corporate purposes of the New Company.

The New Company shall be under no obligation to pay or restore the full benefits under Non-Can policies as originally provided therein, except in the manner and to the extent hereinbefore described; provided, that if title to all or substantially all of the assets of the Accident and Health Department of the New Company shall hereafter be transferred, by voluntary act (other than by statutory merger or consolidation) or by operation of law, to any person who does not in connection with such transfer assume all of the obligations of the New Company to holders of Non-Can Policies, including obligations to restore the benefits thereunder in substantially the manner in this paragraph 14 provided, then and in that event the New Company will be deemed to have fully reinsured and assumed all of the Non-Can Policies, including the obligation to pay in full

all installments of the disability benefits originally provided to persons theretofore entitled thereto.

Assumption of Claims against Old Company

(15) The New Company hereby assumes and agrees to pay in full:

(a) All costs and expenses of the Conservator, including attorney's fees fixed and approved as required by law.

(b) All Federal taxes finally determined to be due from the Old Company. The United States shall have the same legal right of priority and preference with respect to the payment of such taxes out of the assets of the New Company as it had against the assets of the Old Company had these proceedings not intervened, and the New Company agrees that the United States shall have the same remedies against it and its assets with regard to the collection of such taxes as the United States had against the Old Company. No provision of this agreement shall be construed as limiting the operation of the provisions of this subparagraph; nor shall the assets of the Old Company be so valued or the amount of the reserves so redetermined as to prejudicially affect the rights or remedies of the United States. In consideration of the forbearance on the part of the United States at this time to enforce payment of its taxes, all parties hereto agree that the right of the United States to enforce the provisions of the agreement shall be as full and complete as if the United States were named a party hereto.

It is agreed that the foregoing subparagraph (b) shall be embodied in and become a part of the Court's decree of confirmation.

(c) Taxes legally due from the Old Company to any State of the United States, to any County, or to any political subdivision.

(d) Wages, salaries, and pensions legally due to persons employed by the Old Company for services rendered, and current bills and expenses, other than insurance liabilities, in connection with the operation of the business of the Old Company, incurred prior to July 22, 1936, and remaining unpaid, subject of course to any defenses the Old Company may have had thereto.

Assumption of Claims against Conservator

(16) The New Company agrees to indemnify the Conservator against any and all claims and liabilities incurred by him in his capacity as Conservator in connection with the operation of the business of the Old Company, whether in his name as Conservator, in the name of the Old Company, or in the name of the New Company.

Assumption of Claims against Liquidator

(17) In the event the Commissioner shall hereafter be appointed Liquidator of the Old Company, the New Company agrees to assume, and does hereby assume and agree to pay, all costs and expenses of such Liquidator, including attorney's fees, fixed and approved as provided by law. The New Company further agrees to pay, and does hereby agree to pay to the Liquidator for payment to claimants an amount equal to the sum of all claims against the Old Company filed with the Liquidator and finally allowed; provided, however, that the New Company shall not be required to make any payment or payments on account of any claims so filed with the Liquidator except to the extent and in the manner hereinafter provided (but the New Company, with the consent of the Commissioner, may waive the foregoing limitation and anticipate any such payments):

(a) The New Company will, as of the effective date of this agreement, with the approval of or in accordance with the requirements of the Commissioner, establish reserves

against all policies and policy liabilities of the Old Company subject to assumption or reinsurance hereunder (but, with respect to Non-Can Policies, only to the extent described in paragraphs 11 and 13 hereof). If any policy holders or policy claimants shall elect to reject assumption and reinsurance hereunder, the New Company agrees to pay to the Liquidator, immediately after the time for filing claim with said Liquidator shall have expired an amount equal to the reserves so originally established against their policies or claims.

(b) Whenever, pursuant to the provisions of paragraph (14) hereof, any sums are transferred to the special fund for the restoration of benefits under Non-Can Policies, the New Company shall pay to the Liquidator a further sum of money bearing the same ratio to the moneys so transferred as the Non-Can Policies (evaluated as hereinafter provided) whose holders have rejected reinsurance hereunder and upon which claims have been filed in the liquidation proceedings as aforesaid bears to the Non-Can Policies (evaluated as hereinafter provided) whose holders have accepted reinsurance hereunder.

Until such time as the measure of the claims, to the allowance of which holders of Non-Can Policies who file their claim in liquidation proceedings under the laws of the State of California are entitled, shall have been determined to the satisfaction of the Liquidator and he shall so notify the New Company in writing, Non-Can Policies shall, for the purpose of this sub-paragraph, be evaluated on the basis of the percentage established by paragraph 11 hereof of their monthly benefit originally provided, whether or not the holders thereof have accepted reinsurance hereunder.

When the measure of the claim to the allowance of which holders of such policies are entitled, as aforesaid, shall have been determined to the satisfaction of the

Liquidator, and he shall so notify the New Company in writing, Non-Can Policies shall thereafter be evaluated for the purposes of this subparagraph on the basis of allowable claim, whether or not the holders thereof have accepted reinsurance thereunder; but subject to readjustment as hereinafter provided in case of any final determination by the courts of California of any other measure.

In the event payments have been made under any evaluation which is later altered as hereinbefore provided, a recomputation shall be made; and if as a result thereof it appears that there has been an overpayment to the Liquidator, he shall immediately refund to the New Company the amount of such overpayment; but if as a result of such recomputation it shall appear that there has been an underpayment to the Liquidator, the New Company shall adjust such underpayment solely out of funds available for its general corporate purpose, in the manner and upon the terms provided in paragraph 14 hereof for the creation of the special fund where referred to, but in priority to the claims of such fund.

(c) Any remaining amount necessary to pay and discharge the claims as aforesaid shall be paid at the time benefits under the Non-Can Policies are fully restored.

(d) The aggregate of the payments to be made in subparagraphs (a), (b), and (c) hereof, shall not exceed the full amount of claims finally allowed in the Liquidation proceedings as aforesaid. Any moneys paid hereunder and remaining in the hands of the Liquidator after all claims filed with him and finally allowed have been paid, shall be by him returned to the New Company.

(18) Any payments made by the New Company to the Liquidator under the provisions of paragraph 17 hereof may be made in cash or in securities or other assets satisfactory to the Liquidator taken at a valuation satisfactory

to him. If payment is made otherwise than in cash, the Liquidator may, at any time, return any of such securities or other assets to the New Company at the valuation at which the same were taken, and the New Company shall substitute therefor cash or other securities or assets as aforesaid.

Proceeds of Assets Held by Conservator or Liquidator

(19) The conservator, or, if the Commissioner is hereafter appointed Liquidator of the Old Company, such Liquidator shall proceed in such manner and at such time as he deems proper, subject to the provisions of paragraph 20 hereof, to realize upon the assets still held by him as Conservator or as such Liquidator.

In consideration of the various covenants of the New Company herein contained, and for the purpose of protecting holders of Non-Can Policies and of assuring an equitable division of the assets in liquidation among all policy holders and creditors of the Old Company, the Conservator agrees, for himself and for the Liquidator as his successor in title, that the proceeds of any of such assets (other than assets received under the provisions of paragraph (17) hereof) which may hereafter be received by him (or by the Liquidator as his successor in title) shall be used in the manner and only in the manner hereinafter in this paragraph 19 described; and a lien or charge is hereby established upon said proceeds accordingly:

(a) Said proceeds and any part thereof may be used by the Conservator or Liquidator for the payment of any of his costs or expenses of administration, including attorney's fees fixed and approved as provided by law, and any claims having preference in the liquidation proceedings by the laws of the United States or by the laws of the State of

California; and thereupon the obligation of the New Company to pay such costs, expenses, or claims shall be released pro tanto.

(b) In the event benefits under Non-Can Policies shall not theretofore have been fully restored as provided in paragraph 14 hereof, a portion of the remaining proceeds (but not exceeding the amount required to provide complete restoration of the benefits under Non-Can Policies) in the ratio which exists between the Non-Can Policies (evaluated as provided in sub-paragraph (b) of paragraph 17 hereof) whose holders have accepted reinsurance hereunder, and all Non-Can Policies (evaluated as provided in subparagraph (b) of paragraph 17 hereof), whether their holders have accepted reinsurance, or have rejected reinsurance hereunder, and have filed claims in the liquidation proceedings, shall be paid to the New Company, and by it transferred to the special fund described in paragraph 14 hereof.

In the event payments have been made hereunder any temporary evaluation which is later altered as hereinbefore permitted, a recomputation shall be made; and if as a result thereof, it appears that there has been an underpayment from the Liquidator, he shall immediately adjust such underpayment from funds in his hands; but if as a result of such recomputation it shall appear that there has been an overpayment from the Liquidator, the New Company shall repay to the Liquidator from the special fund established pursuant to paragraph 14 hereof when and as there are sufficient moneys therein, (but in priority to the rights of holders of Non-Can Policies who have accepted reinsurance hereunder to restoration of their benefits), the amount of such overpayment.

(c) Any portion of such proceeds remaining after making the payments described in subparagraphs (a) and (b)

hereof shall be used to pay and discharge claims filed with the Liquidator and finally allowed.

(d) Any portion of such proceeds remaining after making the payments described in subparagraphs (a), (b), and (c) hereof shall be paid to the New Company for the purposes of the special fund described in paragraph 14 hereof, to the extent the same may be required to provide full restoration of the benefits under Non-Can Policies.

(e) Any portion of such proceeds remaining after making the payment described in subparagraphs (a), (b), (c) and (d) hereof shall be disposed of by the Liquidator in the manner provided by law.

Mutualization and Disposition of Stock of New Company

(20) Neither the Conservator, nor, if one be appointed, the Liquidator, of the Old Company, shall dispose of any of the stock of the New Company except as follows:

(a) At any time between July 1, 1946 and January 1, 1948, and thereafter so long as the Conservator or a Liquidator of the Old Company may continue to hold any or all of said stock, ten percent (10%) of the holders of participating policies of life insurance entitled to vote at a policy holders' election on a proposal for voluntary mutualization of the New Company, whether those reinsured hereunder or those issued by the New Company (each policy holder for this purpose being regarded as one person regardless of the number of policies owned or amount of insurance held) may request the New Company to create an Appointing Committee as hereinafter provided to exercise the duties and functions hereinafter specified in respect of a proposed voluntary mutualization of the New Company, in accordance with the laws of the State of California in effect at the time of said request, or, if said laws then so permit, of any one or more departments thereof. Such request shall specify the

department or departments of the New Company desired to be mutualized.

Upon the receipt of such request the New Company shall create an Appointing Committee consisting of the then President of the Association of Life Insurance Presidents, the President of Leland Stanford Jr. University, and the Provost of the University of California at Los Angeles, or persons occupying similar positions if their or any of their titles shall have been changed. In the event any one or more of such persons shall refuse or be unable to act, the remaining member or members shall fill the vacancy or vacancies thereby created by their appointment in writing of another person or persons of similar position and standing. If all of said persons refuse or are unable to act, the Court or any Judge thereof shall, on the application of the Commissioner, designate an Appointing Committee consisting of three (3) persons of similar position and standing. Said Appointing Committee, acting through not less than a majority of its members, shall designate a Price Determination Committee of not less than three and not more than five (5) persons skilled in matters of insurance company valuation, which committee, acting through not less than a majority thereof, shall determine whether in their opinion the proposed voluntary mutualization of the New Company, or of the department or departments thereof specified in said request can then be practicably accomplished having due regard to the interests of all persons interested in the New Company. If it be determined that such mutualization is not then practicable no further steps shall be taken in connection with a possible mutualization of the New Company under the provisions of this subparagraph until at least six months after the date of such determination. If in the opinion of a majority of the members of the committee such mutualization is then practicable, the committee shall determine the proper price to be paid upon such mutualization and appro-

priate terms of payments thereof; said determination shall not be made, however, prior to January 1, 1947.

If, at the date of the appointment of such committee the New Company shall have in force Participating Life Insurance written subsequent to the effective date of this agreement in an amount in excess of its Non-Participating Life Insurance written during the same period, one-half (½) of such excess shall, for the purpose of fixing the proper price to be paid (but for no other purpose) be deemed to be, and shall be valued as, Non-Participating Life Insurance. If at the time of such appointment, there shall have been transferred from the Participating Department in accordance with the provisions of sub-paragraph (d) of paragraph 6 hereof, less than ten percent. (10%) of the then accrued earnings described therein, or if there shall have been transferred to the Participating Department any working capital pursuant to the provisions of subparagraph (c) of said paragraph 6, any unpaid balance thereof shall, for the purpose of fixing the proper price to be paid (but for no other purpose) be deemed to be a debt then due and matured. Said Committee shall in its report to the New Company include a plan of mutualization of the New Company, or of the department or departments thereof specified in said request of the policy holders. Such plan shall specify, in addition to any other relevant matters, the price to be paid, the terms of payment, and the persons by whom and the manner in which the right to vote the stock of the New Company is to be exercised pending complete payment of the purchase price. In this connection the said Committee, if it deem it advisable, may provide in the plan for the creation of a voting trust, designate the initial trustees, and make provision for the appointment of their succesors. Unless the benefits under Non-Can Policies have theretofore been fully restored and claims against the Liquidator fully paid, such plan shall further provide that such mutualization shall not affect the

provisions of paragraph 17 or of paragraph 14 hereof or the right of holders of Non-Can Policies to the restoration of benefits from the sources and in the manner therein provided.

The New Company agrees that within sixty (60) days after the making of such report (unless said report shall be to the effect that mutualization is not then practicable) it will mail copies thereof to all of its policy holders entitled to vote upon such plan or plans of mutualization if submitted according to law. If within one hundred twenty (120) days after the mailing of such notice, ten percent. (10%) of the policy holders entitled to vote upon any such plan or plans (each policy holder being for this purpose regarded as one person regardless of the number of policies owned or amount of insurance held) shall request in writing the submission thereof, the New Company will promptly submit the same in accordance with the laws of the State of California then in effect. The Conservator for himself and for any successors in the ownership of said stock claiming under him in any manner other than through a sale of said stock pursuant to the provisions of subparagraph (d) hereof agrees to consent and hereby consents as the holder and owner of the stock of the New Company to such plan of mutualization. In the event said mutualization plan is adopted, the Conservator, or a Liquidator as aforesaid, shall dispose of such stock in accordance with such plan. The expenses of the foregoing proceedings including costs, fees and expenses of the Price Determination Committee, shall be borne by the New Company, and unless the proposed plan of mutualization is consummated, shall be charged to the Participating Department thereof.

In the event the Price Determination Committee has been appointed as herein provided prior to January 1, 1948, said Committee shall have the power to extend the time within which mutualization may be effected hereunder

for such period or periods of time as it may deem necessary for the orderly completion of mutualization proceedings as herein provided.

(b) If at any time prior to the expiration of the option to mutualize a plan of merger, consolidation, reorganization or reinsurance of the New Company is presented to the New Company, or to the Conservator or Liquidator, which in the opinion of the Board of Directors of the New Company cannot be consummated without the elimination of the provisions for mutualization herein contained, the new Company may create an Appointing Committee in the same manner as though the proceeding were under subdivision (a) of this paragraph. Said committee, acting through not less than a majority of its members, shall designate a committee of not less than three nor more than five persons, skilled in matters of insurance company administration and management. The committee so designated shall, acting through not less than a majority of its members, determine whether or not such plan of merger, consolidation, reorganization or reinsurance is practicable and desirable, having due regard to the interests of all persons interested in the New Company. If the committee determine that such plan is practical and desirable, it shall determine a reasonable time which should be allowed for the consummation of the plan. Thereupon the New Company with the written approval of the Conservator or Liquidator, if then there be one, may submit to a vote of the policy holders (voting in the manner then prescribed by the laws of the State of California relating to voluntary mutualization) a proposal to suspend the mutualization provisions of this agreement for the time fixed by the committee, which proposal shall contain a brief description of the plan. If a majority of the policy holders so voting (but not less than ten percent. (10%) of those entitled to vote) vote in favor of the proposal, said provisions for mutualization shall be

suspended for the time so specified and for the sole purpose of consummating the particular plan; and said plan may be consummated within said time free from said provisions and as though no such provisions had ever been contained in this agreement; but unless said plan be consummated within such time said provisions ipso facto shall become fully effective as though there had been no suspension thereof.

The New Company shall, however, at least fifteen (15) days before any vote of policy holders is called under the provisions of this subparagraph, give written notice to each of its General Agents of the intention to call or take such vote. Such notice shall be deemed sufficiently given if and when it is deposited in the United States mails in a properly stamped container, addressed to such General Agent at his latest address appearing on the records of the New Company.

(c) At any time while the stock of the New Company is held by the Conservator or the Liquidator and has not been sold by him the Old Company shall have the right to pay to the Conservator or to the Liquidator the full amount then required by the New Company to complete the restoration of Non-Can benefits and also the amount required by the Conservator or Liquidator to complete the payment of all his claims and liabilities. In the event the benefits on Non-Can Policies shall have been fully restored from earnings of the New Company, contributions of the Old Company, or its shareholders, or otherwise, and all expenses of and claims against the Conservator or Liquidator of the Old Company have been fully paid, the Conservator or such Liquidator shall, upon order of the Court, distribute the stock then held by him in the manner provided by law; provided, however, that if such distribution is made prior to the expiration of the option to mutualize granted in sub-

paragraph (a) of this paragraph 20, the distributees and their successors in the ownership of said stock, shall remain bound, until the expiration of said option, to the aforesaid consent to any mutualization plan of the New Company proposed in accordance with the provisions of subparagraph (a) of this paragraph 20.

The Conservator or Liquidator shall cause to be endorsed upon the certificates evidencing the ownership of such stock an appropriate legend giving notice of the said option to mutualize; and the New Company shall cause a similar legend to be endorsed upon all certificates into which the same may be transferred prior to the expiration of said option.

(d) In the event the Conservator or Liquidator shall at any time determine that conditions are such as to require a sale of said stock, or any thereof, for the protection of the estate in conservation or liquidation, the New Company, or its policy holders, he may sell the same upon order of the Court made after a proper showing of the necessity for such sale upon a full hearing, of which hearing notice shall be given to such parties as the Court may determine are interested therein, and in such manner as the Court may direct.

(e) It is the purpose, spirit, and intent of this agreement that unless the provisions for mutualization are eliminated pursuant to the provisions of subparagraph (b) of this paragraph 20, the stock of the New Company shall not be sold or disposed of prior to the full restoration of benefits under Non-Can Policies except by proceedings for mutualization, so long as a reasonable probability of completing restoration of benefits under Non-Can Policies shall continue; and also, to the end that benefits under Non-Can Policies may be restored as early as practicable, the New Company declares that it will be its policy, at all times while

its stock is held by the Conservator or Liquidator, so far as is reasonably practicable in the ordinary and reasonable conduct of its business to endeavor to write new Non Participating insurance in an amount equal to or in excess of the amount of new Participating Insurance written by it.

(f) If the provisions of this paragraph 20, or of any one or more of the subparagraphs hereof, should be contrary to law or illegal or void, then such paragraph, subparagraph, or subparagraphs, shall be null and void, and shall be deemed separable from the remaining covenants and agreements in this agreement contained; and shall in no way affect the validity of any of the remaining provisions of this agreement.

Agents

(21) The New Company hereby assumes all obligations of the Old Company under agency contracts, provided the other party thereto accepts assumption of his contract by the New Company and agrees to continue bound thereby: provided, however, that the New Company shall not assume or be bound by any agreement or agreements which the Old Company may have made with agents with respect to the payment of commissions on any policies after lapsation. For the purpose of determining Agent's commissions, the reinsurance of policies of the Old Company under this agreement shall be deemed a continuance of existing policies, and not the writing of new insurance by the New Company.

Moratorium

(22) A Moratorium shall be and is hereby imposed upon all cash surrender values and policy loans (except loans for the purpose of paying premiums due or to be due within thirty (30) days of the loan date on the same policy

or on policies of any form (issued with respect to the same person) for a period expiring November 22, 1936: and provided, that the period or extent of this moratorium may be extended or restricted from time to time by ex parte order of the Court made on the application of the Commissioner.

The provisions of this paragraph shall not, however, apply to any increases in values that are accumulated from premium payments or loan repayments which are received subsequent to the effective date of this agreement.

During such priod as this moratorium is in effect, the cash surrender option of all policies of the Old Company shall be considered as non-existent, except as provided above, and all policy holders who do not pay their premiums and who are entitled under their policies to a guaranteed value, will be restricted to the automatic non forfeiture value (properly adjusted for any policy indebtedness and accrued interest thereon) under the policy.

Notice

(23) The New Company shall mail as promptly after the making of the order approving this agreement as shall be reasonably practicable to the insured named in all policies and supplementary contracts of the Old Company in force at the effective date of this agreement, and any assignees thereof of record, a copy of this agreement, as executed, to which the New Company may attach its certificate of reinsurance and assumption, inserted in an envelope, first class postage prepaid, addressed to the name and address of each of the persons aforesaid last shown upon the records of the Old Company. There shall also be included therewith a notice referring to the provisions of paragraph 24 hereof with respect to the manner in which election or rejection of the reinsurance and assumption hereby contained must be manifested. By "assignees of record" is

meant assignees appearing upon the records of the Old Company at its Home Office.

Election of Policy Holders and Claimants and the Effect Thereof

(24) Policy holders and policy claimants of the Old Company may elect to accept or reject the reinsurance and assumption hereunder of his policy, contract, or claim at any time within seventy-five (75) days after the entry of the order approving this agreement. The filing with the New Company after the entry of the order of the Court approving the agreement of any claim or proof of loss shall constitute an acceptance of this agreement and a waiver of any right to reject the same. Any policy holder or policy claimant who shall fail to notify the New Company, in writing, of his rejection within said period shall automatically be deemed to have assented to and become bound by this agreement, and entitled to the benefits hereof.

The filing of a claim with the Liquidator shall, unless such claim is withdrawn within seventy-five (75) days after the entry of the order of the Court approving this agreement, be deemed a rejection of such reinsurance and assumption. The New Company may nevertheless, with the consent of the Commissioner, and upon such terms as the New Company in its sole discretion may desire to impose, permit the withdrawal of a rejection whether or not the period for election herein fixed shall have expired, and permit the person so withdrawing his rejection to accept the reinsurance and assumption herein contained.

Any person electing to accept the reinsurance and assumption herein contained shall thereby be deemed to have entered into a novation with the New Company, and to have released the Old Company from all claims, liabilities, or obligation with respect to his policy or policy claim hereby assumed or reinsured, whether wholly or partially assumed or reinsured.

Conservator Not Personally Liable

(25) No personal liability on the part of Samuel L. Carpenter, Jr. is assumed under this agreement, but he is bound by the provisions of this agreement only in his capacity as such Conservator or as Liquidator of the Old Company. All undertakings and obligations herein set forth as undertakings or obligations of the Conservator are made only in his said capacities and to such extent as he had authority to make the same, and the Conservator makes no warranty of his authority to make the same.

Liability of New Company Limited Hereby

(26) It is understood that the New Company does not assume any liability of any character or description whatsoever of the Old Company except as and to the extent in this agreement expressly provided, and the provisions of this agreement shall be a complete and adequate defense by the New Company to any action, other than an action to enforce the express provisions of this agreement, which may be brought by any policy holders, policy claimants, creditors, or stockholders of the Old Company.

Assignability of Agreement

(27) This agreement and all rights, duties, and obligations hereunder shall inure to the benefit of and be binding upon the respective parties hereto, their several heirs, executors, administrators, successors, and assigns.

Approval of the Court

(28) This agreement shall not become binding upon any party hereto unless and until it shall have been approved by an order of the Court; and when so approved shall constitute an independent agreement, superseding all prior agreements; and also an amendment of the agreement of

July 22, 1936, relating to the reinsurance by the New Company of the business of the Old Company in such manner that said agreement, as amended, shall read in its entirety in the language of this agreement.

In Witness Whereof, the parties hereto have executed this agreement as of July 22, 1936, at the hour of one o'clock P. M. Pacific Standard Time, but in fact on the 4th day of December, 1936.

PACIFIC MUTUAL LIFE INSURANCE COMPANY,

By A. N. KEMP,
Its President.

Attest: RUSSELL HARRIMAN,
Its Secretary.
"New Company"

(Seal)

SAMUEL L. CARPENTER, JR.

Insurance Commissioner of the State of California, as Conservator of The Pacific Mutual Life Insurance Company of California.

(Corporate Seal)

The undersigned, Samuel L. Carpenter, Jr., as Insurance Commissioner of the State of California, does hereby give his written consent to and approval of the foregoing Rehabilitation and Reinsurance Agreement.

SAMUEL L. CARPENTER, JR.,

As Insurance Commissioner of the State of California.

APPENDIX G

Report of Price Determination Committee and pertinent portions of Plan of Mutualization

APPENDIX G

Report of Price Determination Committee and pertinent portions of Plan of Mutualization

Report of Pacific Mutual Price Determination Committee to Pacific Mutual Life Insurance Company.

The undersigned, having been duly designated a Price Determination Committee under and in accordance with the provisions of paragraph 20(a) of the Rehabilitation and Reinsurance Agreement made and entered into as of July 22, 1936, between Pacific Mutual Life Insurance Company, a California corporation, and Samuel L. Carpenter, Jr., Insurance Commissioner of the State of California, as Conservator of The Pacific Mutual Life Insurance Company of California, a California corporation, and in pursuance of requests made thereunder by more than ten per cent (10%) of the holders of participating policies of life insurance entitled to vote at a policyholders' election on a proposal for voluntary mutualization of said Pacific Mutual Life Insurance Company and specifying the Participating and Non-Participating Life Departments of said Corporation as the departments desired to be mutualized, and having entered upon and performed the duties of such Committee pursuant to said agreement, now make this, their unanimous report, to said Pacific Mutual Life Insurance Company.

The undersigned Committee have determined and hereby report that in their opinion the question for their determination, namely, "whether in their opinion the proposed voluntary mutualization of the New Company [Pacific Mutual Life Insurance Company] or of the department or departments thereof specified in said request can then be practicably accomplished, having due regard to the interests of all persons interested in the New Company

[Pacific Mutual Life Insurance Company]," should be answered in the affirmative, and the Committee hereby so answer said question.

The Committee submit herewith and incorporate herein a Plan of Mutualization of said Pacific Mutual Life Insurance Company, as set forth in the pages following.

In the judgment of the Committee, the Plan adequately protects the rights and interests of the insurer, Pacific Mutual Life Insurance Company, of each class of its policyholders and of all interests represented by the Insurance Commissioner of the State of California as holder of the beneficial interest in all the issued and outstanding shares of stock of said Corporation, and said Plan will be fair and equitable in its operation. The Committee have fixed the price to be paid for said shares after full consideration of all matters, both present and prospective, including pertinent provisions of said Rehabilitation and Reinsurance Agreement, bearing upon the value of said shares, and in the judgment of the Committee said price is fair to all interests. The Plan provides for full restoration of all benefits under Non-Cancellable Accident and Health policies as provided in said Rehabilitation and Reinsurance Agreement before any of said purchase price is paid; and the Plan provides for payment of said purchase price only in the event that after its accomplishment the Corporation will remain in possession of requisite and satisfactory reserves and in safe and efficient financial condition. The foregoing statement does not, however, purport to summarize or restate the Plan, to which reference is necessary for its full details and significance.

Pending the adoption and approval of said Mutualization Plan as therein provided, the time within which mutualization may be effected under said Agreement is hereby extended for the period during which the question of adoption and approval of the Plan is pending, and if said

Plan is adopted and approved, the time within which mutualization may be effected thereunder is hereby extended to and including December 31, 1983.

Dated: April 4th, 1950.

Pacific Mutual Price Determination Committee

HORACE R. BASSFORD

ALBERT J. HETTINGER, JR.

RAY D. MURPHY

ALVA J. MCANDLESS

Chairman.

Plan for Voluntary Mutualization of Pacific Mutual Life Insurance Company.

This Plan for voluntary mutualization of Pacific Mutual Life Insurance Company has been formulated by the Pacific Mutual Price Determination Committee under the authority and in accordance with the provisions of paragraph 20(a) of the Rehabilitation and Reinsurance Agreement entered into as of July 22, 1936, by and between Pacific Mutual Life Insurance Company and Samuel L. Carpenter, Jr., as Insurance Commissioner of the State of California, and as Conservator of The Pacific Mutual Life Insurance Company of California. The general purpose of this Plan is to determine the price for which and to prescribe the procedure by which Pacific Mutual Life Insurance Company, if said Plan is duly approved and adopted, shall purchase and cancel all the outstanding shares of its capital stock and be converted from a stock corporation into a nonstock mutual life and disability insurance corporation conducted for the benefit of its members who shall be the policyholders of the Participating and Non-Participating Life classes.

The beneficial interest in said outstanding shares of stock is presently reserved to the Insurance Commissioner of the State of California as Liquidator of the Old Company. The liability of the Old Company under the Non-Cancellable Accident and Health insurance policies issued by it was reinsured and assumed by Pacific Mutual Life Insurance Company at the varying percentages of their stated benefits and under the terms and conditions set forth in paragraphs 10 and 11 of said Rehabilitation and Reinsurance Agreement.

Certain words and phrases as used in this Plan have the following meaning:

Pacific Mutual Life Insurance Company is a California corporation authorized to transact and transacting the business of life insurance and disability insurance in California and elsewhere. It is hereinafter sometimes referred to as "The Corporation."

The Pacific Mutual Life Insurance Company of California is a California corporation, now in liquidation, and the predecessor in the transaction of insurance business of Pacific Mutual Life Insurance Company. It is herein and hereinafter sometimes referred to as "Old Company."

The Insurance Commissioner of the State of California became the Conservator of the Old Company by virtue of an order made and entered by the Superior Court of the State of California in and for the County of Los Angeles on August 11, 1936. Said Insurance Commissioner became the Liquidator of the Old Company by virtue of an order made and entered by said Superior Court on February 3, 1937. He, or his successor in office from time to time, is hereinafter referred to as the Insurance Commissioner, Conservator or Liquidator, respectively.

Wherever the term "Non-Cancellable Accident and Health insurance policies" or similar term is used herein, it refers to the "Non-Can Policies" as defined in said Rehabilitation and Reinsurance Agreement.

"Restoration of Non-Cancellable Accident and Health benefits" (sometimes hereinafter referred to simply as "restoration") means full restoration of said benefits, including deferred restoration balances, with interest, as provided in paragraph 14 of said Rehabilitation and Reinsurance Agreement.

I.

Purchase Price.

A. The price to be paid by the Corporation for said outstanding shares is three million dollars ($3,000,000)

with interest and subject to further augmentation as hereinafter provided, all to be paid in one sum (unless divided to comply with the possibility provided for in Section VII hereof). In the event that restoration of said Non-Cancellable Accident and Health benefits is accomplished prior to January 1, 1973, said sum of three million dollars ($3,000,000) shall be increased by an additional sum of two hundred fifty thousand dollars ($250,000) for each full calendar year by which the date of completion of restoration antedates December 31, 1973.

B. Said sum of three million dollars ($3,000,000) shall bear simple interest from December 31, 1948, until paid. Any additional sum added to said price if and by virtue of the fact that restoration is completed before January 1, 1973, shall bear simple interest from the date of completion of restoration until payment of the purchase price. The rate of all such interest shall be in each calendar year the stated interest rate (i.e., the interest rate stated on the face of the instrument or coupon attached thereto) of the furthest maturity United States Government bonds, publicly held and quoted and having a stated interest rate, which were outstanding at the end of the preceding calendar year, as determined for this purpose by the Treasurer of the Corporation.

II.

Source of Payment and Provisos with Relation Thereto.

A. For the purpose of accumulating a fund to be used in payment, at least in part, of the purchase price, including interest, computed as above stated, for said shares, the board of directors of the Corporation shall, as soon as practicable after the close of each calendar year beginning with the year 1949, cause to be set aside in a Special Surplus Fund created for this purpose five per cent (5%) of the net profits of the Participating De-

partment for such year, excluding, however, that part of the net profits allocable to contracts reinsured under said Rehabilitation and Reinsurance Agreement. Net profits for this purpose are net profits from whatever source (not thus excluded), before dividends, but after charging thereto the cost of acquisition of new Participating business, and after taking into consideration taxes, gains or losses on the sale or other disposition of assets, and such reasonable adjustment in the value of any assets, or reserves for anticipated losses thereon, or otherwise, as the board of directors of the Corporation may from time to time establish, and after deducting therefrom the amount of interest which is added for that year to the Special Surplus Fund, as provided in paragraph B of this Section. Credits from profits into this Special Surplus Fund shall continue until the purchase price for said shares, with interest as specified, has been paid in accordance with Section IV of this Plan, subject to the qualification that the Fund at no time shall exceed the then maximum purchase price as provided herein including interest, less the amount of the capital of the Corporation, and any such excess shall be credited back to the general surplus of the Participating Department.

B. Simple interest equal to the stated interest rate of the furthest maturity United States Government bonds, publicly held and quoted, which were outstanding at the close of the preceding calendar year, as determined for this purpose by the Treasurer of the Corporation, shall each year be added to said Special Surplus Fund from the net profits of the Participating Department and shall be accounted for as a part of said Fund.

C. Said Special Surplus Fund shall be considered and treated as part of the surplus of the Participating Department but may not be distributed or disbursed except as provided in this Plan, or as needed to pay policy obli-

well, A. Crawford Greene, Silas H. Palmer and Wallace K. Downey, as Voting Trustees under the authority of the Pacific Mutual Voting Trust Agreement dated April 4, 1938, entered into by and between said Voting Trustees or their predecessors in interest, and by Samuel L. Carpenter, Jr., as Conservator or Liquidator of The Pacific Mutual Life Insurance Company of California and as "Depositor" under said Pacific Mutual Voting Trust Agreement, and by Pacific Mutual Life Insurance Company. The Insurance Commissioner of the State of California as Liquidator of the Pacific Mutual Life Insurance Company of California is the owner of the beneficial interest in said shares. By its terms said Pacific Mutual Voting Trust Agreement of April 4, 1938, shall immediately terminate upon the adoption of any plan for the mutualization of the Corporation, except as to the extent such plan may otherwise provide. The certificates representing said shares of stock have been issued in or transferred to the names of said trustees under said Pacific Mutual Voting Trust Agreement and show thereon that they were issued pursuant to that said Agreement and such fact is also indicated on the books of the Corporation. Upon the effective date of this Plan, therefore, the Voting Trust set up in said Pacific Mutual Voting Trust Agreement of April 4, 1938, shall immediately terminate and end. The said shares of stock, upon being distributed to the Conservator or Liquidator as provided in said Pacific Mutual Voting Trust Agreement of April 4, 1938, shall be immediately disposed of by said Conservator or Liquidator by transfer to the Voting Trustees of the new Voting Trust hereinafter provided and established, and the certificates therefor shall show that said shares are held pursuant to said new Voting Trust Agreement and such fact shall also be noted on the books of the Corporation. From that time on, all of said shares of stock shall be held and disposed of by said Voting Trustees, or their

successors, upon the terms and conditions of said New Voting Trust Agreement.

B. During the period while this Plan is in effect and pending the payment of said purchase price, a Voting Trust of said shares shall be established and maintained in the form appended hereto as hereinafter in this Section set forth. The following individuals are designated as initial Voting Trustees:

Victor H. Rossetti
Harvey S. Mudd
Rufus B. Von Kleinsmid
Colbert Coldwell
A. Crawford Greene
Silas H. Palmer
Allard A. Calkins
Herbert Hoover, Jr.
Wallace K. Downey

Wallace K. Downey is named herein because he is now the Insurance Commissioner of the State of California, but if, as, and when his successor becomes such Insurance Commissioner such successor shall become the Voting Trustee under this Plan as initial Voting Trustee or otherwise in place of the said Wallace K. Downey.

Said new Voting Trust Agreement shall be in the form appended to and made a part of this Plan, and marked "Appendix—Form of New Voting Trust Agreement."

C. If by reason of any provision of law or otherwise said Voting Trust should fail or be terminated contrary to its terms, such failure or termination shall not adversely affect the balance of this Plan, but in such event said shares shall be returned to the Depositor who shall hold, use, and exercise all of the rights of owner thereof and dispose of such shares, all subject to said Rehabilitation and Reinsurance Agreement and in accordance with said Plan; provided

that he shall in such event, if and to the extent that it shall be lawful, create a new Voting Trust with the same Voting Trustees and upon such of the terms hereinabove provided as may be legally permissible and shall transfer said shares to said Voting Trustees to hold and dispose of said shares in accordance therewith.

If at any time before completion or failure of the mutualization as herein provided, the Voting Trust provided in this Section III shall fail or terminate so as to leave no Voting Trustees acting and qualified for the performance of the powers and duties conferred upon them hereunder, and if the Insurance Commissioner is prevented by any provision of law from establishing a voting trust to take the place of the Voting Trust established by this Plan, the Insurance Commissioner shall himself perform the functions and duties of the Voting Trustees as set forth herein, and particularly, without limiting the generality of the foregoing, their functions and duties enumerated in paragraph D of this Section III and in paragraph D of Section II.

D. It is the policy of the Corporation, as declared in paragraph 20(e) of said Rehabilitation Agreement, in so far as reasonably practicable in the ordinary course of business and for so long as such policy may be anticipated to have the effect of accelerating restoration, to write at least one-half of its new life insurance, other than Group insurance, each year as Non-Participating insurance. In the event that, prior to restoration of said benefits to the extent of ninety per cent (90%) of the difference between the full benefit amount and the amount originally assumed, the Corporation in each of three (3) successive calendar years does not write at least forty per cent (40%) in face amount (or, if there is no face amount, in commuted value) of its new life insurance, other than Group insurance, as Non-Participating insurance, the Trustees shall

appoint from the directors of the Corporation a Committee of not less than three (3) nor more than five (5) members who shall as promptly as possible make a study and written report thereon to the Trustees showing (1) the effect of such departure from the declared policy upon (a) the progress toward completion of restoration, (b) the ultimate price for the shares and time of payment of the same, and (c) the general good of the Corporation, and (2) the justification for such departure from the declared policy. The Trustees shall then decide whether in the circumstances such justification existed, and if not, what action, if any, they should take at the next election of directors.

IV.

Effectuation of Mutualization.

(Payment for Shares; Surrender and Cancellation of Certificates; Amendment of Articles of Incorporation.)

A. When, as, and if, after restoration, the financial condition of the Corporation shall permit making payment for said shares in accordance with the provisions of paragraph D of Section II hereof, and the other conditions set forth in the Plan, precedent to the payment of the purchase price, shall have been met and fulfilled, the Corporation shall thereupon become obligated to purchase said shares, and the board of directors shall authorize and direct the Treasurer of the Corporation to pay to the order of the Insurance Commissioner of the State of California, as Liquidator of The Pacific Mutual Life Insurance Company of California, the price for said shares, including interest, as specified in Section I of this Plan. The board of directors shall cause the Articles of Incorporation of the Corporation to be duly amended in the follow-

ing particulars: Articles Four, Five and Seven as they now read, or the present substance of them if they should have been amended, shall be deleted. The following shall be substituted for said Article Four:

> "Four: This corporation shall be a nonstock life and disability insurance corporation, conducted for the benefit of its members who shall be the policyholders of the Participating and Non-Participating Life classes."

The following shall be substituted for said Article Seven:

> "Seven: This corporation expressly reserves the right to amend its articles of incorporation from time to time in such manner and for such purposes as may at the time be permitted by law."

B. Upon receipt of the payment referred to in paragraph A of this Section, the Liquidator shall notify the Trustees under the Voting Trust established under Section III of this Plan (being also the Trustees under any second voting trust created under Section VII hereof) of the fact of such payment, and said Trustees shall promptly vote for or consent in writing to the amendments of the Articles of Incorporation of the Corporation referred to in said paragraph A, and thereupon shall deliver to the Liquidator the Certificates for the said shares of stock duly endorsed. The Liquidator shall thereupon endorse said certificates and surrender them to the Treasurer of the Corporation, who shall cause them to be cancelled.

C. When all of said outstanding shares have been acquired and cancelled, and the certificate of amendment of the Articles of Incorporation has been duly filed as provided by law, this Plan shall be deemed to be completed and shall terminate, and the Corporation shall be and thence-

forth become a nonstock life and disability insurance corporation conducted for the benefit of its members, as provided by law, with due account taken of the right of recovery to the surplus of the Participating Department provided in paragraph E of Section II above.

VI.

Failure of Consummation of Mutualization.

In the event that the price of said shares shall not have been paid, as herein provided, by December 31, 1983, this Mutualization Plan shall be considered to have failed, the Voting Trust established pursuant to Section III hereof shall terminate and said shares of stock shall be returned to the Liquidator as therein provided, and any amounts then standing in said Special Surplus Fund shall revert to the general surplus of the Participating Department of the Corporation.

Appendix.

Form of New Voting Trust Agreement.

Voting Trust Agreement.

This Agreement, made the ..... day of ....., 195.., between Victor H. Rossetti, Harvey S. Mudd, Rufus B. Von Kleinsmid, Colbert Coldwell, A. Crawford Greene, Silas H. Palmer, Allard A. Calkins and Herbert Hoover Jr., as parties of the first part, and (Name of Insurance Commissioner of the State of California), as Conservator or Liquidator of The Pacific Mutual Life Insurance Company of California (who in his capacity as such Conservator or Liquidator, but not otherwise, is hereinafter usually referred to as "Depositor"), as party of the second part, is entered into under the following circumstances:

Pacific Mutual Life Insurance Company (hereinafter usually referred to as "Corporation") is a California corporation qualified to do and doing life and disability insurance business in approximately forty (40) states of the United States. All of the capital stock of the Corporation was, immediately prior to the execution of this agreement, owned and held by the Depositor.

The Corporation is a party to a certain Rehabilitation and Reinsurance Agreement dated as of July 22, 1936 (hereinafter sometimes referred to as "Rehabilitation Agreement"), under which it acquired, with the approval of the Superior Court of the State of California, substantially all of the assets and business of The Pacific Mutual Life Insurance Company of California (hereinafter sometimes referred to as "Old Company").

Pursuant to the Rehabilitation Agreement, a Plan of Mutualization of the Corporation has been adopted and approved and is now in effect.

In view of the provisions of the Rehabilitation Agreement and of the Mutualization Plan and the objects and purposes thereof and in the belief that such objects and purposes will be facilitated and expedited and the interests of all parties concerned, including policyholders and creditors of both the Old Company and the Corporation, will be benefited if the legal title to stock of the Corporation be transferred to voting trustees of established character and ability, in order that they may exercise the rights of stockholders in the control of the Corporation; reserving to the Depositor, however, the entire beneficial interest in such stock, with those considerations in mind, and in order to accomplish those purposes, the parties hereto agree as follows:

FIRST: There is hereby established a Voting Trust of the stock of Pacific Mutual Life Insurance Company in accordance with the terms and provisions of this Agree-

ment. The original trustees hereunder other than the Depositor shall be the parties of the first part, and the Depositor shall be the party of the second part. Said persons and their successors selected as hereinafter provided are herein sometimes referred to as the "Trustees."

SECOND: The Depositor agrees to assign and does hereby assign to the Trustees ten thousand (10,000) shares of the capital stock of the Corporation, being all of its authorized or issued stock. The Depositor agrees forthwith to deliver to the Trustees the stock certificates representing such shares duly endorsed for transfer. The Depositor agrees to pay or cause to be paid any and all taxes payable with respect to the transfer of any stock assigned to the Trustees under the provisions of this article Second.

THIRD: The certificates representing any shares of stock at any time held by the Trustees hereunder shall be issued in or transferred to the names of the Trustees hereunder and shall show that they are issued pursuant to this Agreement and such fact shall also be noted on the books of the Corporation.

FOURTH: All of said stock, and all payments made to and properties received by the Trustees as owners of such stock shall be received by the Trustees in trust, and shall be held, distributed, or otherwise disposed of, by the Trustees as provided in this Agreement. While this Agreement continues in effect the Trustees shall have full legal title to all shares of the stock of the Corporation deposited with or held by them hereunder, and shall be entitled to exercise with respect thereto all rights and powers of every name and nature which the Depositor had, except as may be otherwise herein expressly provided.

It is expressly agreed that the Trustees have an interest in all shares of stock deposited with or held by them here-

under; and, during the period this Agreement continues in effect, the power evidenced hereby shall be irrevocable.

FIFTH: This Trust, unless sooner terminated in accordance with the provisions of this paragraph, shall continue and be irrevocable for a period of thirty (30) years from its effective date and thereafter during such lawful extensions of time of not more than five (5) years each as may be granted by the Insurance Commissioner of the State of California. Within such time, and any such extension thereof, it shall expire and terminate upon the occurrence of the earliest of the following events, and not sooner: (a) upon the filing with the Secretary of State of the State of California of a copy of the Certificate of Amendment of the Articles of Incorporation of the Corporation pursuant to the provisions of paragraph C of Section IV of said Mutualization Plan, or (b) at such time as the Board of Directors of the Corporation shall determine that such Plan has failed in accordance with Section VI of said Plan and that said Plan is, therefore, abandoned, and shall notify the Trustees to that effect, or (c) in any event upon the termination of any second voting trust created in accordance with Section VII of said Plan.

Upon the termination of this Trust, any shares held in this Trust shall revert to the persons entitled thereto by law; that is to say, (a) to the trustees under the second voting trust, if any, created in accordance with Section VII of the Mutualization Plan if the transfer to the trustees thereof is then required by law, or, (b) in any other case, to the Liquidator or his successor in interest. Upon any such transfer the Trustees may require the payment of a sum sufficient to reimburse them for any charge for expenses accruing in connection with any such delivery and for all expenses incurred or paid by the Trustees in the performance of this Trust.

SIXTH: It is expressly covenanted and agreed that except as herein or in said Mutualization Plan expressly provided, no sale, assignment, transfer, pledge, mortgage, bequest, gift, or statute of distribution or descent, shall in any manner affect the trusts hereby created or the shares of stock of the Corporation held hereunder, or affect, release or otherwise prejudice any of the shares of stock held by the Trustees hereunder nor the right, title, interest, and estate of the Trustees therein; but this Agreement until the termination hereof as herein provided shall be and continue in full force and effect notwithstanding any attempted sale, assignment, transfer, pledge, mortgage, bequest or gift of said shares held hereunder and notwithstanding the operation of any statute of distribution or descent by reason of the death of any person having any interest in the shares held hereunder.

SEVENTH: The Trustees, during the continuance of this Agreement, shall be vested with and shall possess and shall be entitled to exercise in their discretion all the rights and powers of an absolute owner of the stock held by them hereunder, including (without limiting the generality of the foregoing) the unrestricted right in their discretion to vote, and to give or withhold any consent for or in connection with any matter whatsoever, including (without limiting the generality of the foregoing) the election of directors of the Corporation, the amendment of its Articles of Incorporation, in any manner (except as limited by the remainder of this article), the issue, incurrence, assumption, or guaranty or undertaking or any other obligation for the payment of any indebtedness secured or unsecured, the mortgage, pledge or other encumbrance of any of its property or assets, the liquidation, dissolution, or winding up of the Corporation, the consolidation or merger of the Corporation with or into any other corporation, the reorganization of the Corporation, the reinsurance of any or all

of its business, or the sale of all or substantially all of its properties and assets as an entirety, and the acquisition of properties, assets, and business or stock or securities of any other corporation or other party, all for such consideration, whether cash, securities or other properties, as the Trustees in their discretion may determine.

Provided, that the Trustees shall not vote for or give their consent to any change in the capital structure of the Corporation or to the issuance of any new stock of the Corporation; and shall not give their consent to any liquidation, dissolution, or winding up of the Corporation, any consolidation or merger of the Corporation with or into any other corporation, any reinsurance of all or substantially all of its business, or any sale of all or substantially all of its properties and assets as an entirety, without the written consent of the Depositor, or his successor in interest, nor in violation of the terms, spirit, or intent of the Rehabilitation Agreement or of said Mutualization Plan.

The Trustees shall, and by accepting the trust hereunder, they agree that they will, take such steps as are in their power to the end that all of the provisions of the Rehabilitation Agreement and of said Mutualization Plan are fully and faithfully carried out and particularly that the covenants therein contained on the part of the Depositor are performed, and that they, the Trustees, will vote for or consent in writing to the amendments of the Articles of Incorporation of the Corporation provided for in said Mutualization Plan if and when submitted to them in accordance with said Plan.

EIGHTH: The Depositor, or his successor in interest, shall, if he then be a Trustee hereunder, at all times be ex official Chairman of the Trustees with the right to vote at all meetings of Trustees. The Trustees shall select from their own number a vice-chairman, a secretary and such

other officers as they deem necessary or proper. They may adopt their own rules and methods of procedure. The action of a majority of the Trustees expressed from time to time at a meeting of the Trustees duly called and noticed, or by writing with or without meeting, shall in every case constitute the action of all of the Trustees and have the same force and effect as though all of the Trustees had voted for or consented to said action. The Trustees may vote in person or by proxy the shares held hereunder at any and all meetings of the stockholders of the Corporation, but no such proxy shall be valid unless executed by a majority of the Trustees, nor shall any such proxy be given to any person or persons not a Trustee or Trustees hereunder.

In voting the stock held by them hereunder, the Trustees shall exercise their best judgment to the end that the affairs of the Corporation shall be properly managed, but it is understood and agreed that no Trustee incurs any responsibility by reason of any matter or things done or omitted under this Agreement, except for his own individual malfeasance, and no Trustee shall be responsible for the act or omission of any other Trustee hereunder.

None of the Trustees, while continuing to serve as such, may act as a director or officer of the Corporation and the Trustees shall not vote for any one or more of their number as directors of the Corporation.

Any Trustee may purchase, or be the holder, beneficiary or assignee of, or the insured under, any policy of insurance issued by the Corporation. The Trustees each for himself agree that they will not themselves borrow from, buy from, sell to, or accept any compensation for services from the Corporation; provided, this Agreement shall not extend to or prohibit:

(a) The borrowing by any Trustee upon a policy of life insurance upon his own life in accordance with the terms of such policy;

(b) The acceptance by any governmental officer of any fees, expenses, compensation, or emoluments properly chargeable by him in his capacity as such officer;

(c) The acceptance of fees for services as Trustees hereunder or reimbursement or indemnification for costs or expenses incurred in acting hereunder as hereinafter specifically permitted, or any other moneys he is entitled to receive under the provisions hereof.

NINTH: The Trustees shall have the right to appoint, employ, and remove and pay reasonable compensation to such agents, attorneys, accountants and actuaries as they in their discretion may deem necessary for the purpose of enabling them to carry out the terms and provisions of this Agreement, with such powers and duties as the Trustees may from time to time confer on them respectively; and neither the Trustees, nor any of them, shall be liable in any way for any act of commission or omission of any such agent, attorney, accountant or actuary. The opinion of such legal counsel or of counsel for the Depositor shall be full protection to the Trustee for anything done or permitted to be done by them or any of them in good faith and in accordance with such opinion.

The Trustees shall be entitled to no compensation for their services hereunder, except a reasonable fee for attendance upon meetings and expenses reasonably incurred in traveling to and returning from such meetings. The Trustees may from time to time fix the amount of such fee for each day or fraction thereof reasonably required in traveling to, attending upon, or returning from such meetings; but no Trustee shall receive an aggregate of more than $2500 as compensation for such services in any one calendar year.

The Depositor, or his successor in interest, while serving as a Trustee hereunder shall be entitled to receive

reimbursement for his expenses, as aforesaid, but shall be entitled to no compensation for his services as a Trustee hereunder.

The Depositor, for himself and his successor in interest, agrees from time to time, upon the request of the Trustees, to pay or reimburse them for all expenses, including compensation of Trustees, and to indemnify them for and against any and all claims and liabilities, incurred by them, or any of them, in connection with or growing out of this Agreement or the bona fide discharge of their duties hereunder, including expenses, claims, and liabilities incurred by any agent of the Trustees, and in the absence of such payment and reimbursement by the Depositor, the Trustees shall be entitled to be paid or reimbursed out of any moneys coming into their hands hereunder.

Under the terms of the Rehabilitation Agreement hereinbefore referred to, the Corporation has agreed to pay the costs and expenses of the Conservator and Liquidator of the Old Company, which will include the obligation of the Depositor hereunder. Furthermore, the Corporation is of the opinion that this Trust Agreement is and will be to its advantage and to the advantage of its policyholders. The Corporation has therefore agreed that it will advance for the Depositor all items of expense or indemnification described in the last preceding paragraphs; the Depositor has agreed that the Trustees shall reimburse the Corporation for any such advances out of any moneys coming into their hands hereunder as a result of any dividends or distribution or other proceeds of any securities held by them hereunder; and the Corporation has agreed to look only to such right of reimbursement for the repayment of any such advances.

TENTH: The Depositor, as herein provided, retains a beneficial interest in the shares of stock which are the

subject matter of this Voting Trust. He holds and agrees to hold such beneficial interest in place and in lieu of said shares of stock and subject to the same conditions and restrictions now appertaining to the holding of said shares. Specifically the Depositor agrees that he will not sell, transfer, or dispose of said beneficial interest in violation of the terms of said Rehabilitation Agreement or Mutualization Plan. Any person succeeding to the ownership of all or any part of said beneficial interest, whether by virtue of succeeding to the office of Insurance Commissioner, or Liquidator of the Old Company, or otherwise, shall as such successor in interest be bound by all of the provisions hereof and entitled to all of the advantages hereof as fully as if he had signed this instrument.

ELEVENTH: Any Trustee may resign at any time by giving to the other Trustees written notice of his resignation and the time at which it shall become effective.

The Depositor is a Trustee hereunder by virtue of his ownership of a beneficial interest in the subject matter of this Trust; and he shall remain a Trustee hereunder only so long as he retains a beneficial interest in any of the shares then constituting the subject matter hereof. Each successor of the Depositor in his capacity as Conservator or Liquidator of the Old Company, during such time as he retains a beneficial interest in any of the shares then constituting the subject matter hereof, shall, at all times during the continuance of this Trust, be and remain a Trustee hereunder.

Any other vacancy among the Voting Trustees arising after completion of the designation and appointment of the initial Voting Trustees, whether arising by death, inability to act, resignation, disqualification, or refusal to accept office as a Trustee, shall be filled by a majority of the remaining Trustees, though less than a quorum,

or by a sole remaining Trustee, by written appointment filed with the Insurance Commissioner of the State of California and with the Corporation; provided, that the term of office of any Trustee elected to fill a vacancy arising by reason of the Depositor or his successor in office, as aforesaid, ceasing to own the beneficial interest requisite to the retention of his office, as aforesaid, or by reason of any refusal or failure of the Depositor or his successor to accept, or continue in, office as a Voting Trustee, shall continue only until the Depositor or his such sucessor shall regain the requisite beneficial interest or accept office as a Trustee hereunder.

Any Trustee appointed as aforesaid shall, upon filing with the Chairman of the Voting Trustees a written acceptance of such appointment, automatically be vested with all estates, titles, rights, powers and privileges of a Trustee hereunder as fully as if originally named herein.

TWELFTH: All notices given to the Depositor or his successor in interest may be given by mail addressed to him at his latest address filed with the Trustees. The giving of any such notice may be waived by the Depositor or his such successor in interest either before or after the time for giving the same.

All notices to the Trustees may be given by mail to the then Trustees addressed to them at their respective addresses then on file with the Insurance Commissioner of the State of California. The giving of any notice to any Trustee may be waived by such Trustee either before or after the time for giving the same.

THIRTEENTH: The stock certificate or certificates from time to time representing the shares of stock of the Corporation held hereunder shall be lodged with the Chairman of the Trustees as custodian, subject to the order of the Trustees, and the terms of this Agreement.

FOURTEENTH: If at any time a tax is payable by the Trustees in respect of the ownership of any stock held by them hereunder, and the Trustees shall lawfully be required to pay the same, the Trustees shall pay the same and shall be reimbursed for any payments so made by the Depositor in accordance with the provisions of Article Ninth.

FIFTEENTH: Whenever the term "Trustees" is used herein, it is intended that such term shall include the Trustees for the time being in office, whether original or successor; and whenever the term "Corporation" is used herein, it is intended that the term shall include Pacific Mutual Life Insurance Company and any successor or successors thereto.

SIXTEENTH: The Trustees are authorized and empowered to construe this Agreement and their construction of the same made in good faith shall be final, conclusive and binding upon the Corporation and all persons interested therein.

SEVENTEENTH: The invalidity or nonenforceability of any term or provision of this Agreement shall in no wise impair or affect the remaining valid terms and provisions hereof which shall remain in full force and effect.

EIGHTEENTH: The provisions of this Agreement shall inure to the benefit of and be binding upon the original Trustees and all future Trustees hereunder; and also the original Depositor and all of his successors in interest. The relationship created hereby is one of Trustee and *cestui que* trust, and no other or different relationship is intended to be hereby created between the parties hereto.

NINETEENTH: This Agreement may be executed in several counterparts, each of which when so executed shall be deemed to be an original and such counterparts

taken together shall constitute but one and the same Agreement.

TWENTIETH: Prior to the issuance of any certificate to the Trustees representing the stock held by them hereunder, a duplicate of this Agreement shall be filed in the principal office of the Corporation in the State of California.

TWENTY-FIRST: It is one of the primary purposes of this Agreement to assure the full accomplishment of all of the intents and purposes of the Rehabilitation Agreement and said Mutualization Plan in accordance with their terms. The parties hereto therefore declare that no provision of this Agreement is to be construed in any manner which would result in a violation of any of the terms, agreements, or provisions of said Rehabilitation Agreement or of said Mutualization Plan; and if any covenant or agreement provided herein on the part of the Trustees or the Depositor to be performed should be contrary to any express provision of or to the policy of said Rehabilitation Agreement or of said Mutualization Plan, or contrary to any express provision of law, or contrary to the policy of express law, then such covenant or covenants, or agreement or agreements, shall be null and void, and shall be deemed separable from the remaining portions hereof, and shall not affect the validity of the remaining portions of this Agreement.

If a second voting trust is created in accordance with Section VII of the Mutualization Plan and if any of the shares of stock held hereunder are acquired by the Corporation in accordance with the provisions of said Plan, such shares so acquired, together with the voting rights thereof, shall be transferred by the Trustees under this Trust to the trustees under such second voting trust, but only if such transfer should become necessary or requisite

for the effectuation or validity of said Plan or of this Trust.

If the appointment of any Trustee hereunder (either original or successor) shall be unlawful, or void, or subject to avoidance, such appointment shall be null and void and shall not take effect, but his office shall be deemed to be vacant; provided that such disqualification shall have no effect upon the validity of this Agreement or upon the validity of the appointment of any of the other Trustees hereunder, or upon any act or action done or taken by them (notwithstanding such disqualified person shall have purported to join therein), if such act or action could have been validly done hereunder by the Trustees actually concurring therein (disregarding such disqualified person).

TWENTY-SECOND: This Agreement shall take effect upon its execution by the Depositor and by any four of the parties of the first part hereinbefore named. Any one of said parties of the first part not executing this Agreement prior to the time it becomes effective, may nevertheless execute the same, and by such execution become a party hereto and a Voting Trustee hereunder at any time within ninety (90) days after this Agreement becomes effective; but he shall not become such a Voting Trustee unless and until he shall have executed this Agreement within such period of ninety (90) days. No vacancy arising by reason of such failure to execute this Agreement shall be filled by action of the remaining Trustees, as hereinbefore provided, unless the same shall have continued beyond said period of ninety (90) days, or the party so failing to execute this Agreement shall have theretofore filed with the Chairman of the Trustees a written refusal to accept office as such Trustee.

TWENTY-THIRD: (Name of Insurance Commissioner of the State of California), in entering into this Agreement, does so solely in his capacity as Conservator or

Liquidator of The Pacific Mutual Life Insurance Company of California; and he does not intend hereby to and does not assume any personal or individual obligation or liability under any provision of this Agreement; and the parties hereto and all persons dealing with the Trustees agree that they will not assert or seek to assert any claim against him in his individual capacity, but they will look solely to the assets to which he or his successor in office is entitled as such Conservator or Liquidator and to the covenants and obligations of the Corporation as contained herein and in said Rehabilitation Agreement, for the satisfaction of any claims, obligations, or liabilities hereunder.

TWENTY-FOURTH: This Agreement may be designated for brevity "Pacific Mutual Voting Trust Agreement"; and the Trustees hereunder may act under the designation "Trustees under Pacific Mutual Voting Trust Agreement."

In Witness Whereof, the parties hereto have executed this Agreement as of the day and year first above written.

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.....

.....

Parties of the First Part

.....

Insurance Commissioner of the
State of California
Party of the Second Part

Pacific Mutual Life Insurance Company hereby consents to the foregoing Voting Trust Agreement, and agrees to be bound by its terms.

Dated this ..... day of ....., 19..

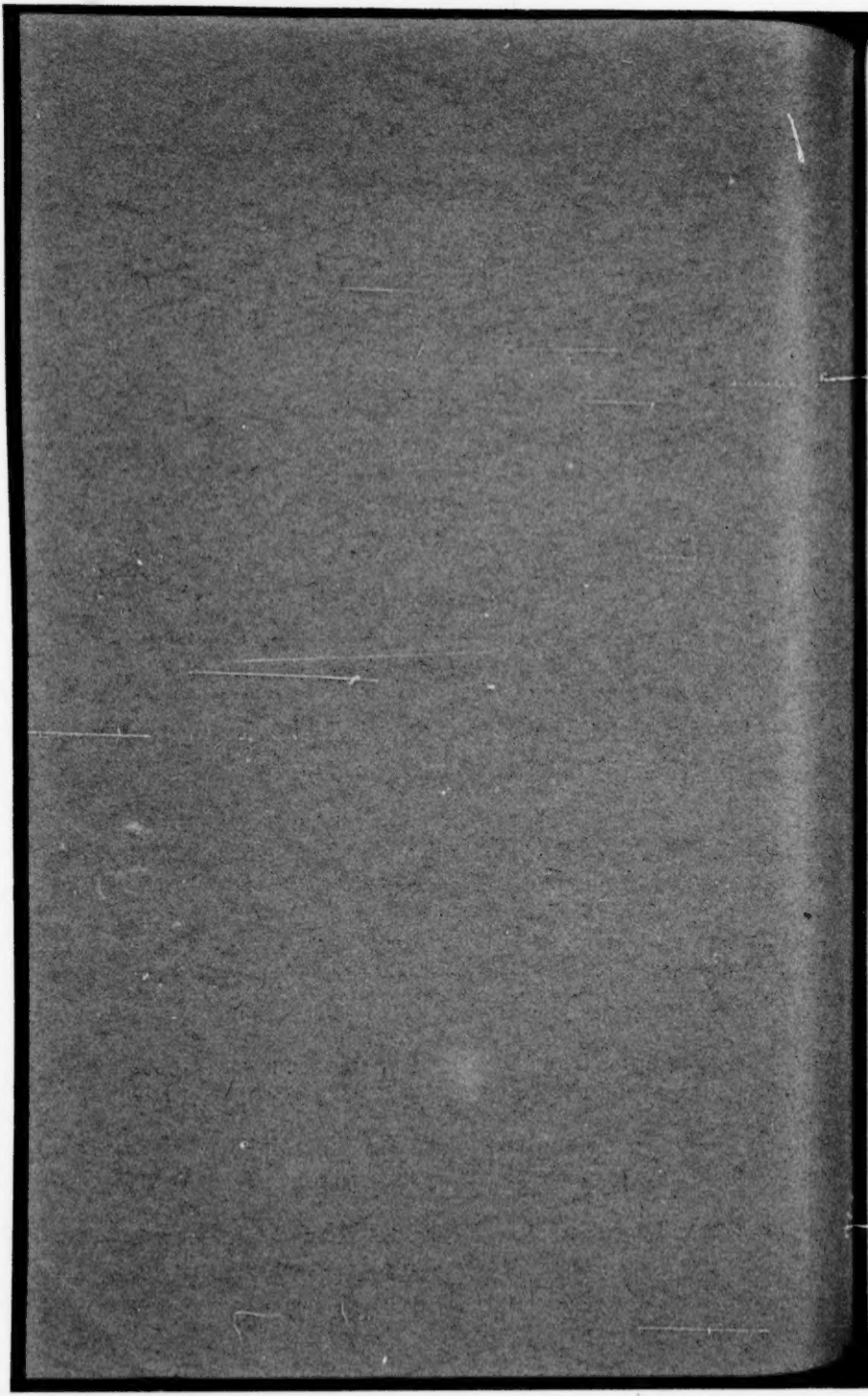
Pacific Mutual Life Insurance Company

By .....
President

And .....
Secretary

APPENDIX H

Judgment appealed from



APPENDIX H

Judgment appealed from

IN THE

SUPREME COURT OF THE STATE OF CALIFORNIA

L. A. No. 23261

THE PACIFIC MUTUAL LIFE INSURANCE COMPANY OF CALIFORNIA, *et al.*, *Appellants,* *vs.* F. BRITTON MCCONNELL, as Insurance Commissioner etc., *et al.*, *Respondents.*	ON APPEAL FROM THE SUPERIOR COURT IN AND FOR THE COUNTY OF LOS ANGELES SUPERIOR COURT No. 579832

The above entitled cause having been heretofore argued, and submitted and taken under advisement, and all and singular the law and premises having been fully considered,

IT IS ORDERED, ADJUDGED AND DECREED by the Court that the

Judgment

of the Superior Court in and for the County of Los Angeles in the above entitled cause, be and the same is hereby affirmed.

Respondents to recover costs on appeal.

I, WILLIAM I. SULLIVAN, Clerk of the Supreme Court of California, do hereby certify that the foregoing is a true

copy of an original judgment entered in the above entitled cause on the 27th day of June, 1955, and now remaining of record in my office.

Witness my hand and the seal of the Court affixed at my office this first day of August, A. D. 1955.

WILLIAM I. SULLIVAN, Clerk

By PAUL DINOIA
Deputy

DEC 22 1955
HAROLD B. WILLEY, Clerk

IN THE

Supreme Court of the United States

OCTOBER TERM, 1955

No. 585

THE PACIFIC MUTUAL LIFE INSURANCE COMPANY OF CALIFORNIA, a California corporation, SAMUEL K. RINDGE, and WILLIAM H. JACK, *Appellants,*

v.

F. BRITTON McCONNELL, as Insurance Commissioner of the State of California, F. BRITTON McCONNELL, Insurance Commissioner of the State of California, as Liquidator of The Pacific Mutual Life Insurance Company of California, and PACIFIC MUTUAL LIFE INSURANCE COMPANY, a California corporation, *Appellees.*

On Appeal From the Supreme Court of the State of California

JURISDICTIONAL STATEMENT

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TABLE OF CONTENTS

	Page
Opinions and Judgment Below	2
Jurisdiction	2
Statutes Involved	4
Questions Presented	4
Statement	
I. Circumstances in Which Questions Arose	6
1. 1936 Proceedings	6
2. Rehabilitation Agreement	7
3. California Mutualization Statutes	8
4. Provisions for Mutualization in Rehabilitation Agreement	9
5. Purposes of Provisions for Mutualization	10
6. Appointment of Liquidator and Transfer of Stock of New Company to Voting Trustees	11
7. Gist of Plan of Mutualization	11
8. Substantive Due Process	12
9. Adoption of Plan of Mutualization	13
10. Procedural Due Process	14
11. Opinions of California State Supreme Court	16
(a) Majority opinion	16
(b) Dissenting opinion of Traynor, J.	17
(c) Dissenting opinion of Carter, J.	17
12. 1936 Case on Review	18
II. Valuation by Guesswork	19
1. Method of Valuation	19
2. Estimates of Earnings Admittedly Speculative	20
3. Rate of Discount Arbitrary	21
4. Confiscatory Character of Method	22
5. Valuation Not Based on Evidence	23
III. The Plan of Mutualization	24
1. Confiscation of $29,000,000	24
2. Deprivation of Incidents of Ownership	27
3. Insuring Control of Management	29

Page

IV. The Compulsion Resulted From the Order of the Insurance Commissioner 32

1. The Rehabilitation Agreement Was, at Most, Binding on the Liquidator 34
2. The Rehabilitation Agreement Derived Its Force From the Order of December 4, 1936 34
3. The Promise in the Rehabilitation Agreement to Dispose of the Stock Was Subject to the Express Condition Precedent That the Plan be First Adopted 35
4. The Plan of Mutualization Expressly Requires the Transfer of the Stock to the New Voting Trustees 36
5. The Order of December 4, 1936 is Part of the Totality of State Action 36

Raising of the Questions Below 37

The Case is within the Jurisdictional Provisions Relied On 42

I. A Proper Case for Appeal Is Presented Because the Order of the Insurance Commissioner Is Legislative in Character 42

II. A Proper Case for Appeal Is Presented Because the Validity Under the United States Constitution of State Statutes, as Construed and Applied by the State Court, Is Involved 43

The Questions Are So Substantial as to Require Plenary Consideration 46

I. Valuation by Speculation 46

II. Valuation as of Present and Payment in Distant Future 48

III. Deprivation of Incidents of Ownership for 35 Years 49

IV. Secs. 11526-7 as Construed 50

V. Mutualization as a Device for Corporate Control 51

VI. Other Substantial Questions 52

Alternative Application for Certiorari 53

INDEX TO APPENDICES

Page

Appendix A. Opinions in the Supreme Court of California 1a

1. Majority Opinion 1a
2. Dissenting Opinion of Traynor, J. .. 14a
3. Dissenting Opinion of Carter, J. 19a

Appendix B. Opinion of the District Court of Appeal 62a

Appendix C. Opinion of the Superior Court 94a

Appendix D. Opinion and Decision of the Insurance Commissioner 125a

Appendix E. Judgment Appealed From 167a

Appendix F. Statutes 168a

1. Insurance Code of California 168a
2. Code of Civil Procedure of California 185a

TABLE OF AUTHORITIES CITED

CASES:

American Dept. Stores Corp., In re, 16 F. Supp. 977 34
Atchison, T. & S. F. R.R. v. Pub. Util. Com., 346 U.S. 346 3
Belden v. Union Central Life Ins. Co., 143 Oh. St. 329 42
Benedict v. City of New York, 98 Fed. 789 48
Bensley v. Mountain Lake Water Co., 13 Cal. 306 ... 48
Breslav v. Light & Power Co., 249 App. Div. 181 ..42, 43
Butler v. Sewer Commissioners, 39 N. J. Law 665 .. 48
Cabot Bank, Appeal of, 26 Conn. 7 45
Capital Transit Co. v. Pub. Util. Com., 213 F. 2d 171 47
Carlson v. Washington, 234 U.S. 103 32
Carpenter v. Pacific Mutual, 10 Cal. 2d 307 ....7, 8, 18, 30
Case v. Los Angeles Lumber Products Co., 308 U.S. 106 34
Cole v. Arkansas, 333 U.S. 196 37
Connecticut Ry. & Lighting Co. v. Palmer, 305 U.S. 493 21

Page

Connecticut Ry. & Lighting Co. v. Palmer, 109 F. 2d 568 21
Consolidated Rock Products Co. v. DuBois, 312 U.S. 510 .....21, 46
Doty v. Love, 295 U.S. 64 3
Fayerweather v. Ritch, 195 U.S. 276 32
Fidelity & Deposit Co. v. Tafoya, 270 U.S. 426 46
Fink v. Cole, 302 N.Y. 216 44
Frank v. Mangum, 237 U.S. 309 37
Hanover Fire Ins. Co. v. Harding, 272 U.S. 494 46
Hansberry v. Lee, 311 U.S. 32 .....16, 32, 46
Jacobs v. United States, 290 U.S. 13 13
Kuhner v. Irving Trust Co., 85 F. 2d 35 21
Lake Erie & W. R.R. v. Pub. Utilities Com., 249 U.S. 422 3
Lord v. Equitable Life Ass. Soc., 194 N.Y. 212 42
Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555 .....13, 49, 50
Mason v. Pewabic Mining Co., 133 U.S. 50 43
McGibson v. Roane County Court, 95 W. Va. 338 .. 48
Murel Holding Corp., In re, 75 F. 2d 941 48
Northern Pacific Railway Co. v. Dept. of Pub. Works, 268 U.S. 39 47
Neblett v. Carpenter, 305 U.S. 297 .....18, 30
Ohio Valley Water Co. v. Ben Avon Borough, 253 U.S. 287 45
Old Colony R.R. Co. v. N.Y., N.H. etc. R.R. Co., 98 F. 2d 670 21
Old Dearborn Distributing Co. v. Seagram-Distillers Corp., 299 U.S. 183 50
Pacific Mutual v. Martin, 369 Ill. 157 8
Postal, etc. Co. v. Newport, 247 U.S. 464 32
Provident Mutual Life Ins. Co. v. University Evangelical Lutheran Church, 90 F. 2d 992 48
Prudential Ins. Co. of America, Application of, 132 N. J. Eq. 170 42
Prudential Ins. Co. of America, In re, 82 N. J. Eq. 335 42
Quaker City Cold Storage Co., In re, 71 F. Supp. 124 34
Rippel v. Prudential Ins. Co. of America, 85 N.J.L. 395 42
Royal Trust Co. v. Equitable Life Ass. Co., 247 Fed. 437 31
Sanborn v. Pacific Mutual Life Ins. Co., 42 Cal. App. 2d 99 35

Page

Seaboard Air Line R.R. v. U.S., 201 U.S. 299 13
S.E.C. v. Central Illinois Securities Corp., 338 U.S. 96 48
St. Joseph Stockyards Co. v. U.S., 298 U.S. 38 45
Standard Oil Co. v. Johnson, 311 U.S. 487 3
Sultan R. & T. Co. v. Dept. of Labor, 277 U.S. 135 .. 3
Terral v. Burke Construction Co., 257 U.S. 529 46
Thomas v. Calif. Emp. Stab. Com., 39 Cal. 2d 501 .. 45
United Fuel Gas Co. v. R.R. Comm., 278 U.S. 300 .. 21
United Railways Co. v. West, 280 U.S. 234 45
United States ex rel. Accardi v. Shaughnessy, 347 U.S. 260 44
United States ex rel. Accardi v. Shaughnessy, 99 L. Ed. Adv. 637 44
United States v. Burnison, 339 U.S. 87 3
United States v. Pink, 315 U.S. 203 30
United States v. Westinghouse Electric & Mfg. Co., (1950) 339 U.S. 261 .....21, 48
Vulcan & Reiter Co., In re, 152 F. 2d 92 36
Washington Gas Light Co. v. Baker, 188 F. 2d 11 .. 47
Waterbury v. The Platt Brothers and Co., 76 Conn. 435 48
Watson Seminary v. Pike County Court, 149 Mo. 57 34
West Ohio Gas Co. v. Pub. Util. Com., 294 U.S. 79 .. 47
Wheatley v. Root, 147 Ohio St. 127 42
Wheeling Steel Corp. v. Glander, 337 U.S. 562 36
Yukon v. Vose, 201 Okla. 376 42

TEXTBOOKS:

Badger and Guthman: Investment Principles and Practices, (3rd ed.) pp. 81, 35 22
Bonbright: The Valuation of Property, Vol. I, p. 261 22
Dewing: The Financial Policy of Corporations, 1953 ed., Vol. 2, p. 1310 .....21, 22
Gaskill, J. F.: Gouge, pp. 152-4, 156-7 19
House Subcommittee on the Study of Monopoly Power, November 30, 1949 52
Poor's Register of Directors and Executives, 1953 ed. 29
Pujo Committee Report, pp. 146-7 32
Report of Association Examination of Pacific Mutual Life Insurance Company, December 31, 1953, p. 45 25
Samuelson: Economics, pp. 128, 132 .....51, 52

Page

Temporary National Economic Committee Monograph # 28, pp. 64-87 32
T.N.E.C. Hearings, February, 1939, Part IV, pp. 1555-7 32

STATUTES:

California Code of Civil Procedure, § 1094.5 ....2, 4, 45

California Insurance Code:

§ 1016 11
§ 1037 11
§ 1037 (e) 11
§§ 1043-1056 .....4, 8, 9
§§ 11,525-11,533 .....4, 9
§ 11,526 .....4, 5, 9, 10, 37, 41, 43, 44, 46, 50
§ 11,526(b) 10, 29, 33
§ 11,527 .....4, 5, 9, 10, 14, 37, 41, 43, 44, 46, 50
§ 11,529.5 28

6 Code of Va., 1950 §§ 38.1-489 to 38.1-495.5 51
Dist. of Columbia Code, 1951 ed, Title 35, § 35-519 .. 51
Book 27, part 2, McKinney's Consolidated Laws of New York § 199 51
6 Minnesota Statutes Annotated, Chapter 61, §§ 61.461 and 61.462 51
New Jersey Statutes Annotated, 17:34-33 to 34-43.7 51
7 Ore. Compiled Laws, Ann., §§ 101-601 to 101-611 51
Page's Ohio Revised Code, Annotated, §§ 3913.01 to 3913.10 51
Purdon's Penn. Statutes, Ann., Title 40, §§ 592 to 595 51
Smith-Hurd Annotated Statutes, Chapter 73, § 647 51
1952 Supplement to South Dakota Code of 1939, §§ 31.1803 to 31.1806 51
United States Code, Title 28, § 1257 (2) 3, 4
United States Constitution, Amendment XIV 5, 6, 37
4 Utah Code Annotated (1953) § 31-8-7 51
14 Vernon's Texas Civil Statutes, Article 21.27 51
4 Williams Tennessee Code Annotated (1934), 1952 Pocket Supplement, §§ 6433.14 to 6433.31 51

IN THE

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No.

THE PACIFIC MUTUAL LIFE INSURANCE COMPANY OF CALIFORNIA, a California corporation, SAMUEL K. RINDGE, and WILLIAM H. JACK, *Appellants,*

v.

F. BRITTON MCCONNELL, as Insurance Commissioner of the State of California, F. BRITTON MCCONNELL, Insurance Commissioner of the State of California, as Liquidator of The Pacific Mutual Life Insurance Company of California, and PACIFIC MUTUAL LIFE INSURANCE COMPANY, a California corporation, *Appellees.*

On Appeal From the Supreme Court of the State of California

JURISDICTIONAL STATEMENT

This is an appeal from a judgment of the Supreme Court of California. The judgment was entered June 27, 1955. A petition for rehearing was denied July 27, 1955. Three justices dissented from both the judgment and the order denying a rehearing.

Appellants submit this statement to show that the Supreme Court of the United States has jurisdiction of the appeal and that substantial questions are presented.

This Statement is filed on behalf of the appellants named in the caption. The other parties who were appellants in the Court below, except Rudolph H. Brand, who is deceased, have filed a separate Statement.

OPINIONS AND JUDGMENT BELOW

The majority and two dissenting opinions in the Supreme Court of California are reported at 44 Cal. 2d 715 and 285 P. 2d 636, and are attached hereto as Appendix A. The opinion of the District Court of Appeal, First Appellate District, Division Two, is reported at 270 P. 2d 584, and is attached hereto as Appendix B. The opinion of the Superior Court and the opinion and order of the Insurance Commissioner are not reported but are attached hereto as Appendix C and Appendix D respectively. The judgment of the state supreme court from which this appeal is taken is attached hereto as Appendix E.

JURISDICTION

(1) Appellant, The Pacific Mutual Life Insurance Company of California, called Old Company, and the individual appellants (who are stockholders of Old Company) filed a petition in the Superior Court for a peremptory writ of mandate, under § 1094.5 of the Code of Civil Procedure of California (Appx. F, p. 185a), to rescind an order of the Insurance Commissioner of California, made September 22, 1950, approving a plan of mutualization for appellee Pacific

Mutual Life Insurance Company, called New Company. The Superior Court denied appellants' petition by a judgment filed June 2, 1952, and entered June 6, 1952. On appeal, the District Court of Appeal affirmed the judgment by a decision filed May 14, 1954. The Supreme Court of California granted a hearing on July 13, 1954, and subsequently entered its judgment affirming the judgment of said Superior Court.

(2) The judgment of the Supreme Court of California sought to be reviewed was dated and entered June 27, 1955. Appellants' petition for rehearing was denied by said Supreme Court without opinion, three justices dissenting, by order entered July 27, 1955. Notice of appeal to this Court was filed with the Clerk of the Supreme Court of California on October 24, 1955.

(3) 28 U.S.C. § 1257 (2) is the statutory provision on which the jurisdiction of the Supreme Court to hear this appeal rests.

(4) The cases believed to sustain the jurisdiction of the Supreme Court are: *Standard Oil Co.* v. *Johnson,* (1942) 316 U.S. 481; and *United States* v. *Burnison,* (1949) 339 U.S. 87; holding that a proper case for appeal is presented where the validity under the United States Constitution of a state statute as construed by the state courts is involved; and *Doty* v. *Love,* (1935) 295 U.S. 64; *Atchison, Topeka & Santa Fe Railway Co.* v. *Public Utilities Commission,* (1953) 346 U.S. 346; *Lake Erie & W. R.R.* v. *Public Utilities Commission* (1919) 249 U.S. 422; and *Sultan R. & T. Co.* v. *Department of Labor,* (1928) 277 U.S. 135; holding that an order of a state administrative body such as the one here in question is legislative in char-

acter and therefore a statute within the meaning of 28 U.S.C. § 1257 (2).

STATUTES INVOLVED

The validity of §§ 11,525-11,533, (particularly §§ 11526 and 11527) of the Insurance Code of California as construed and applied by the California courts in this case, is involved. The validity of the before mentioned order of the Insurance Commissioner, which is a statute within the meaning of 28 U.S.C. § 1257(2), is also involved.

While the validity of §§ 1043-1056 of the Insurance Code of California is not involved in this appeal, and the validity of § 1094.5 of the Code of Civil Procedure of California is also not involved in this appeal, those statutes have a bearing upon the case.

There is no official edition of the statutes of California.

The text of all the before mentioned provisions of the Insurance Code and Code of Civil Procedure of California is set forth in Appendix F.

QUESTIONS PRESENTED

The Plan of Mutualization approved by the Insurance Commissioner provides for the purchase by New Company of all of its outstanding stock. It binds appellants as equitable owners to a sale of the stock at a price determined as of 1948, the payment of which will not be made until the distant future, i.e., between 1971 and 1983, and then only if conditions precedent to the obligation of New Company to purchase the stock shall have been satisfied.

The questions presented are whether the order of the Commissioner approving the Plan of Mutualization and the before mentioned judgment of the Supreme Court of California, and §§ 11526 and 11527 of the Insurance Code of California, as construed and applied in this case, deprive appellants of property without due process of law contrary to Amendment XIV of the Constitution of the United States because:

(1) The Plan of Mutualization fixes the purchase price of the stock in accordance with a valuation thereof arrived at by speculation and guess-work and upon assumptions having no rational basis in law or fact;

(2) The Plan of Mutualization fixes a price for the stock which on its face, and according to the uncontradicted evidence, is grossly inadequate and confiscatory;

(3) The Plan of Mutualization does not provide for the payment of the purchase price of the stock on the basis of its value at the time when the obligation to purchase and pay may arise but permits New Company to buy the stock at a remote future date, at a price equal to the value that the stock was determined to have had in 1948, plus interest at an inadequate and non-compensatory rate, all payable only if, at the time the obligation to pay may arise, the stock is worth many times the purchase price and interest;

(4) The Plan of Mutualization deprives appellants of incidents and benefits of their equitable ownership of the stock, for a period that may extend to 1983, without compensation and without a definite and unconditional obligation to purchase and pay for the stock.

In addition, questions are presented whether, by the order, the judgment and the California statutes, as construed and applied, appellants have been denied their day in Court and deprived of their property without due process of law contrary to Amendment XIV because:

(1) Appellants have not had an opportunity to submit to a judicial tribunal, or any tribunal provided by law, for determination upon its own independent judgment as to law and fact, their claim that confiscation of their property will result if the Plan of Mutualization becomes effective; and

(2) The order of the Commissioner approving the Plan is not supported by substantial or competent evidence and was not based upon a fair and open hearing before an impartial tribunal.

STATEMENT

I

Circumstances in Which Questions Arose

1. 1936 Proceedings

In July, 1936, the Insurance Commissioner found that the reserves of Old Company were insufficient as to non-cancellable accident and health policies, sometimes called "non-cans" and, therefore, Old Company was insolvent within the meaning of the Insurance Code, although it was not insolvent in either the bankruptcy or equity senses of the term. The Insurance Commissioner accordingly filed three proceedings in the Los Angeles Superior Court in which, upon the written consent of the President and the Counsel of Old Company, three orders were made respectively appointing the Insurance Commissioner

Conservator of Old Company, approving a plan of rehabilitation, and appointing the Insurance Commissioner Liquidator of Old Company. Pursuant to these orders, the Insurance Commissioner as Conservator organized New Company, as his agency and instrumentality to rehabilitate the business of Old Company; and transferred to New Company substantially all of the assets of Old Company in exchange for the capital stock of New Company. No new money went into New Company.

The Insurance Commissioner as Conservator held the stock of New Company as trustee for Old Company, its policyholders and creditors (Appx. A, p. 21a).

By August 11, 1936, it became apparent that the three consent orders made on July 22, 1936 were void. On August 11, 1936 the Superior Court, on application of the Insurance Commissioner, made an *ex parte* order appointing the Insurance Commissioner Conservator of Old Company. The order also approved the creation of New Company to rehabilitate the business of Old Company, and directed the Conservator to present a plan of rehabilitation.

On September 25, 1936, the Conservator filed a petition presenting a proposed rehabilitation agreement and asked the Court's approval of the same. On notice and after a hearing, the Court on December 4, 1936 made an order approving the proposed rehabilitation agreement and directing the execution thereof.[1]

2. Rehabilitation Agreement (Ex. 9)

The Rehabilitation Agreement was in form a contract between the Conservator and New Company. The

[1] Appx. A, p. 2a; see *Carpenter* v. *Pacific Mutual* (1937) 10 Cal. 2d 307 (Appeal from order of December 4, 1936).

purpose of the rehabilitation agreement was to remove the technical insolvency caused by the deficiency in reserves by scaling down non-can liabilities; and making provision for their restoration in the future out of a special fund to be created from certain profits of New Company.[2]

On December 4, 1936, following the order of that date, the Conservator and the officers of New Company who as officers of Old Company had consented to the three void orders, joined in executing the Rehabilitation Agreement.

In 1950, at the time of the hearing before the Insurance Commissioner, at the conclusion of which his order herein involved was made, non-can benefits had been restored to the extent of 36% (Ex. 24).[3]

According to the reports of New Company on file with the insurance departments of forty states, and widely published in insurance manuals, by early 1955 non-can benefits had been restored to the extent of 72%.

3. California Mutualization Statutes

§§ 1043-1056 (Appx. F, pp. 177a-185a) of the Insurance Code authorize the involuntary mutualization of the "business" of insolvent companies. §§ 11525 et seq. of the Insurance Code (Appx. F, pp. 168a-177a)

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[2] *Pacific Mutual* v. *Martin* (1938) 369 Ill. 158, applying *Carpenter* v. *Pacific Mutual, supra.*

[3] The record on this appeal consists of four numbered folders and certain numbered exhibits. Reference to "Tr." in this Statement refer to "Reporter's Transcript of proceedings before the Insurance Commissioner," contained in Folio One; "Clk. Tr." to Folder Two; and "Ex." to separate numbered exhibits.

authorizes the voluntary mutualization of solvent companies. A plan of involuntary mutualization, adopted in accordance with the provisions of the Insurance Code, binds all parties including the Company and the stockholders. A plan of voluntary mutualization adopted in accordance with §§ 11,525 *et seq.* is not binding on either the company or the stockholders. The company may refuse to buy and the stockholders may refuse to sell.

§ 11526, governing voluntary mutualization, provides that the plan must (a) be adopted by the Board of Directors; (b) approved by a majority of the stockholders; (c) approved by the Insurance Commissioner; and (d) approved by a majority of the policyholders.

§§ 1043-62, on the other hand, provide for the preparation of the plan by the Conservator or Liquidator of the insolvent company, and its approval by the Superior Court in the exercise of its own independent judgment.

Both sets of mutualization statutes were enacted in 1935, the year before the Insurance Commissioner took over Old Company and proposed the Rehabilitation Agreement.

4. Provisions for Mutualization in Rehabilitation Agreement

The Rehabilitation Agreement undertook to provide for "voluntary mutualization" under §§ 11,526-7 but, at the same time, to make the contemplated plan of mutualization compulsory. Provision was made for setting up a Price Determination Committee subsequent to 1946. (The Conservator was prohibited from selling the stock of New Company held by him as

trustee for the Old Company except subject to the provisions for mutualization.) The Price Determination Committee was authorized to determine after 1946 whether mutualization was "then practicable" and, if it so determined, to prepare a plan of mutualization and report the same to New Company, New Company being obligated, on certain conditions, to submit the same "in accordance with the laws of California then in force." (i.e., §§ 11,526-7 of the Insurance Code)[4]

The Conservator as trustee for the stockholders undertook to give in advance the consent required by § 11,526(b) on behalf of the stockholders to any plan of mutualization P.D.C. might report. The Conservator also agreed that should the plan reported be adopted, he or his successor as Conservator or Liquidator would dispose of the stock of New Company in accordance with the plan.

5. Purposes of Provisions for Mutualization

In the majority opinion of the state supreme court it is said: "The Commissioner apparently concluded that a plan of mutualization which could not be destroyed by future action or non-action of share holders was necessary . . ." (Appx. A, p. 12a).

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[4] The effect of § 11,526 is stated above. § 11,527 is as follows:

"Sec. 11527. *Examination of plan by commissioner: Conditions prerequisite to approval.* The commissioner shall examine the plan submitted to him under the provisions of subdivision (c) of section 11,526. He shall not approve such plan unless in his opinion the rights and interests of the insurer, its policyholders and shareholders are protected nor unless he is satisfied that the plan will be fair and equitable in its operation."

6. Appointment of Liquidator and Transfer of Stock of New Company to Voting Trustees

The Insurance Commissioner was appointed Liquidator on February 3, 1937.[5] At the time no order was made under § 1016 of the Insurance Code, for the dissolution of the Old Company, and no order has since been made. The powers of Conservators and Liquidators are found in § 1037 of the Insurance Code. The only substantial changes made by the order appointing the Conservator as Liquidator were (a) to make applicable the provisions of § 1016 of the Insurance Code permitting dissolution of the Old Company and (b) to provide a procedure for the filing of claims by dissentients and the payment thereof.

The only reasonable inference from the record is that the several Commissioners who have acted as Liquidator have not applied for an order of dissolution because they all wished the Old Company to be in a position either to receive the stock of New Company, or its purchase price in the event of mutualization, and distribute the same to its stockholders.

Legal title to the stock of New Company is in the name of voting Trustees, of whom the Liquidator is one, the Liquidator having on April 14, 1938, transferred the stock to such Trustees by virtue of Subsection (e) added to § 1037 of the Insurance Code in 1937.

7. Gist of Plan of Mutualization

On April 4, 1950, the Price Determination Committee theretofore created, reported the Plan of Mutualization here in question to New Company.

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[5] The Insurance Commissioner *qua* Insurance Commissioner is a formal party. The Liquidator was made a party because, as trustee for Old Company, he refused to bring the proceeding. (Clk. Tr. 4)

The Report stated that P.D.C. had found mutualization was "then practicable." (Ex. 15)

(a) The Plan constitutes a proposal by the New Company to the Liquidator as the holder of the stock of New Company in trust for Old Company, to buy all the capital stock of New Company for $3,000,000 on certain conditions and contingencies provided such conditions and contingencies happen by 1983.

(b) The Plan provides, in the event the restoration of non-can benefits shall be completed before January 1, 1974, there shall be added to the purchase price additional sums of $250,000 for each full year such restoration is accelerated.

(c) The Plan provides for simple interest on the purchase price at the rate carried by the furthest maturity interest-bearing Government bonds outstanding (2½ percent in 1948). No interest is payable unless payment of the purchase price is first made. According to the evidence this will not be until some time after 1973; so that interest, if paid, would be more than 20 percent less than the yield on comparable Government bonds, which pay interest serially.

(d) The Plan provides for the happening of designated conditions before there is any obligation on the part of New Company to pay the purchase price of the stock or interest. (Ex. 15, pars. IID, IVA)

8. Substantive Due Process

(a) The uncontradicted evidence shows that upon the happening of the conditions on which New Company becomes obligated to pay the purchase price of $3,000,000 and the interest provided for, the stock will be worth more than $29,000,000 in excess of the purchase price and interest. (See *post*, pp. 24-27)

(b) The uncontradicted evidence also shows that should New Company become obligated to pay the accretions of $250,000 annually, New Company would receive an annual gift of $1,750,000 of the stockholders' money. (See *post,* p. 27)

(c) As a matter of law, the interest rate provided for is uncompensatory. (See *Jacobs* v. *U. S.* (1933), 290 U.S. 13; *Seaboard Air Line Railroad Co.* v. *U.S.* (1922) 261 U.S. 299; *Louisville etc. Bank* v. *Radford* (1935) 295 U.S. 555)

(d) The Plan of Mutualization, by its terms, deprives Old Company, the equitable owner of the stock of New Company, of the incidents of ownership for a period of thirty-five years, meanwhile putting New Company in the hands of hostile persons, whose discretion is made unreviewable. (See *post,* pp. 27-30).

9. Adoption of Plan of Mutualization

On May 15, 1950, without any investigation of its own, and upon inquiry of certain officers only as to whether the Plan was fair to the *policyholders,*—not the stockholders,—the Board of Directors of New Company voted to adopt the Plan. (Ex. 19)

On June 15, 1950, a majority of the Voting Trustees executed written consents to the Plan on behalf of the stockholders, expressly reciting in the consents that the trustees had given no consideration to the merits of the Plan. (Ex. 21)

Other than the purported consents of the Voting Trustees, there was no consent given by or on behalf of the stockholders unless, as held by the state supreme court, consent was given by the terms of the Rehabilitation Agreement, (which we deny, see *post,* pp. 45-6).

On June 16, 1950, New Company submitted the Plan to the Insurance Commissioner, in his character as an administrative officer. (Ex. 1)

After a hearing, the Insurance Commissioner on September 22, 1950, rendered an Opinion and Decision in which, virtually in the language of § 11,527 of the Insurance Code of California (*ante* p. 9, n. 4) he "found as a fact that the rights and interests of the New Company, its policyholders, and the holder of its shares are protected under the terms of the Plan hereinabove referred to, and that the Plan will be fair and equitable in its operation", and concluded "that the Plan is lawful in all respects and meets all requirements of the Insurance Code." (Appx. D, p. 145a)

The Insurance Commissioner accordingly approved the Plan.

10. Procedural Due Process

(a) PDC, two of the four members of which had ties of interest with the management, valued the stock by guesswork as a result of secret investigations of which no record was kept. (Clk. Tr. 18-19, 66-68, 95-96; *post,* p. 19ff.) All the evidence in the record was taken in the proceedings before the Insurance Commissioner. (Appx. B, p. 81a)

(b) Because of his conflicting duties as Liquidator and as an administrative officer, the Insurance Commissioner was not impartial; and not only did he act as a judge in his own case, but he failed to exercise his own discretion in approving the Plan. He approved it merely because he concluded that PDC had not acted arbitrarily, although he had before him only a portion of the data on which PDC acted. (Appx. C, p. 122a; *post* p. 44)

(c) The record of the proceedings before the Insurance Commissioner was judicially reviewed only to determine whether the Insurance Commissioner in approving the plan had acted arbitrarily or abused his discretion and not to determine whether in the independent judgment of the Superior Court, or any court, the plan was fair and equitable. (Appx. A, p. 13a, Appx. B, p. 92a, Appx. C, p. 105a)[6]

No evidence was received in the Superior Court (Appx. B, p. 81a).

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[6] The District Court of Appeal says in its opinion:

> "• • • the power and duty to determine the value and price of the stock was lodged in the Price Determination Committee and not in the Insurance Commissioner, by the Rehabilitation and Reinsurance Agreement." (Appx. B, p. 86a)

The appellate court also says:

> "• • • It does not appear • • • that any committeeman or valuer • • • was guilty of partiality, bad faith, or misconduct in their appraisals • • •." (Appx. B, p. 91a)

The majority opinion of the California Supreme Court says:

> "There is no merit in plaintiffs' claim that the record before the commissioner does not support his approval of the plan. The price determination committee consisted of men highly skilled in matters of insurance company valuation, and they were assisted in the formulation of the plan by Joseph Christman, associate actuary of the Metropolitan Life Insurance Company of New York, two Fellows of the Society of Actuaries, and numerous trained supervisory and clerical employees. Experts testified that the price fixed for the purchase of the stock was fair, that the provisions relating to the time and manner of payments were necessary for the safety and stability of the new company, that the proposed plan gave due regard and protection to the rights of all persons interested in the new company and would be fair in its operation." (Appx. A, pp. 13a-14a)

11. Opinions in California State Supreme Court

(a) **Majority opinion** (Appx. A, pp. 1a-14a).

The Majority opinion decides:

1. The order of the Insurance Commissioner does not deprive Old Company or its stockholders of vested rights because it constitutes only a permit to New Company to buy its stock (Appx. A, p. 13a).

2. There was substantial evidence to support the order of the Insurance Commissioner because two members of the P.D.C. and its chief actuary testified the Plan was fair and equitable and protected the rights of all parties (See note 6, *ante* p. 15).

3. The Insurance Commissioner acted as a judge in his own case, but he was justified in so doing by necessity (Appx. A, pp. 6a-7a).

4. The courts were entitled to review the proceeding before the Insurance Commissioner only to determine whether the Insurance Commissioner had acted arbitrarily or abused his discretion (Appx. A, p. 13a).[7]

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[7] Much is said in the majority opinion about the order of December 4, 1936, being res judicata, but the opinion limits the application of res judicata to the advance consent of the conservator and does not extend it to the proceedings before the Insurance Commissioner. In view of the reservations in Paragraph 20 (f) of the Rehabilitation Agreement and the reservation of jurisdiction at the foot of the order of December 4, 1936, (see *post*, p. 35) res judicata could not, consistently with due process, have been extended further. (See *Hansberry* v. *Lee*, (1940) 311 U.S. 32). Moreover, res judicata could not, consistently with due process, have been made applicable even to the advance consent of the Conservator. (See *post*, pp. 45-6.)

(b) **Dissenting opinion of Traynor, J.** (Appx. A, pp. 14a-18a).

Traynor, J. was of the opinion that by the construction the majority opinion placed on the Rehabilitation Agreement and the provisions of the Insurance Code, "the shareholders of the Old Company", were deprived of the "veto power" they otherwise would have had and were obliged to look to the Commissioner rather than to the Superior Court for protection of their interests.[8]

(c) **Dissenting opinion of Carter, J.** (Appx. A, pp. 19a-61a)

The dissenting opinion of Carter, J. is too comprehensive for brief statement. Two points, however, may be noted. Carter, J. insisted appellants were entitled

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[8] The following is from the opinion of Traynor, J.:

"The importance to the shareholders of the old company of having the Court independently pass upon the fairness of the plan of mutualization is demonstrated by the facts of this case. The trial Court clearly indicated that had the decision been his, the plan would not have been approved; if the shareholders were entitled to his independent judgment, their rights have been prejudiced by his failure to exercise it. This case is not one involving only the mutualization of a solvent insurer, since if it were, the shareholders would have the power to protect their interests by withholding their consent to the plan of mutualization. (Ins. Code, Sec. 11526, subd. (b).) In fact, the business of an insolvent insurer is being mutualized pursuant to a rehabilitation agreement that has deprived the shareholders of the old company of the veto power they otherwise would have, and under the holding of the majority opinion they must look to the Commissioner rather than to the Court for the protection of their interests. (Ins. Code, Sec. 11526, subd. (c), 11527.) Although the Legislature recognized that approval by the Commissioner is sufficient when all of the interested parties are in a position to protect their own interests, it also provided that Court approval is essential when they are not. (Ins. Code, Sec. 1051.)" (Appx. A, p. 15a)

under both the State and Federal Constitutions to full judicial review of the order of the Insurance Commissioner (Appx. A, pp. 50a-57a). Referring to the order of the Insurance Commissioner, Carter, J. said: *"It surely must be crystal clear to everyone who can think that such an outrageous confiscation of property without due process of law has never before taken place in this State."* (Appx. A, p. 57a)

12. 1936 Case on Review

The 1936 proceedings in which the Insurance Commissioner was appointed Conservator of Old Company were before this Court in *Neblett* v. *Carpenter,* 305 U.S. 297 (1938), on certiorari to the Supreme Court of California, *Carpenter* v. *Pacific Mutual,* 10 Cal. 2d 307 (1937).

In its opinion in the 1936 case, this Court was at pains to point out that Old Company's difficulties were of a temporary nature, not involving true insolvency. (305 U.S. at 299)

In its opinion in the 1936 case, the state supreme court said that Old Company was *"technically insolvent as that term is defined in the Insurance Code but, by no means bankrupt."* (10 Cal. 2d at 325)

In his opinion in the 1936 case, the trial judge said:

> "I have gathered from the evidence in this case a firm conviction that the Pacific Mutual Life Insurance Co. of California is not stricken by any serious or ruinous condition. *In the commercial sense of the word, it is not insolvent; it was able to meet its obligations as they fell due up to the time the Commissioner took it over, and would have been so able for years in advance had it not been taken over,* but the Law has prescribed certain standards or reserves to be set up, for the protection of the public who deal with life insur-

ance companies. That standard, applied by the State Commissioner, in the exercise of his duty, revealed the fact last Spring that the *reserves were inadequate; therefore, under the artificial definition of insolvency, the company was insolvent.*" [Not officially reported but printed on pp. 1504-5 in the Transcript on Appeal to the California Supreme Court which is part of the Record in this Court in *Neblett* v. *Carpenter, supra.*

See also "Gouge" (1938) by J. F. Gaskill, pp. 152-4, 156-7.

The procedures for mutualization in the Rehabilitation Agreement were not submitted for the consideration of this Court or the Supreme Court of California in the above mentioned case. Indeed there were no allegations in the pleadings in the 1936 case relating to such procedures for mutualization. (Appx. A, pp. 46a-47a).

The Plan of Mutualization approved by the Insurance Commissioner involved in this case has not heretofore been before any court or tribunal, except the Insurance Commissioner and the courts below in the proceedings now before this Court.

II

Valuation by Guesswork

The record affirmatively shows without conflict that the purchase price of the stock was arrived at by speculation and guess-work and upon assumptions having no rational basis.

1. Method of Valuation

The Price Determination Committee valued Old Company's stock (a) by first determining that non-can policies would not be fully restored until 1974;

(b) by then ascertaining or speculating on a pattern of prospective earnings of New Company beginning in 1974; (c) by then arbitrarily assigning figures for prospective earnings for each year from 1974 to 2000, and a lump sum from 2000 to perpetuity; (d) and by then arbitrarily discounting to December 31, 1948, said prospective earnings from 1974 forward at the rate of 10% compounded annually. (Ex. 28, pp. 2, 8, 10)

By this method the stock was valued at $3,000,000 as of 1948, but under the terms of the Plan there was no obligation on the part of New Company to pay until after 1974 (see *post*, pp. 24-26).

2. Estimates of Earnings Admittedly Speculative

Exhibit 28, which is the backbone of P.D.C.'s valuation, states:

> "These estimates are, of course, subject to great uncertainty. They are the result of an extensive series of calculations which have been carefully carried out, but which *involve assumptions as to happenings in the distant future which may or may not be realized.*" [Ex. 28, p. 8]

Mr. McAndless stated that the Committee's estimates of earnings far in the future were subject to substantial uncertainty and therefore the Committee was unable to estimate earnings for particular years and accordingly attempted to determine a pattern of earnings which the Committee thought would be too low for some years and too high for others and hoped that the deviations from the norm might offset each other so that the figures arbitrarily assigned for particular years would be substantially accurate (Tr. 341, 296).

The best that Mr. Hettinger, the other member of P.D.C. who testified, could say was that the Committee's estimates of earnings were not estimates of specific amounts that would be earned in particular years but were estimates of the future pattern of earnings and the Committee thought deviations from the pattern in one direction would be likely offset by opposite deviations at other times. (Tr. 388-9)

It is not too much to say that estimates of earnings so made are not only without a rational basis but are fantastic.[9]

3. Rate of Discount Arbitrary

Exhibit 28 states that the *ten percent rate was "fixed on after reviewing available literature* on this subject, particularly Professor Bonbright's book on 'The Valuation of Property', Dewing's 'The Financial Policy of Corporations', and Badger's 'Valuation of Industrial Securities'." (Ex. 28, p. 12)

At the time the valuation was made by P.D.C. the most authoritative literature on the subject consisted of the opinion of this court in *Consolidated Rock Products Co.* v. *DuBois* (1941), 312 U.S. 510.

It does not appear from the record whether that piece of literature was consulted. It does appear, however, that the *DuBois* case was not followed by P.D.C. in determining the rate of discount.

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[9] *Connecticut Railway and Lighting Company* v. *Palmer* (2d Cir. 1940), 109 F. 2d 568, 570 (aff'd. 1941, 311 U.S. 544); *Connecticut Railway and Lighting Company* v. *Palmer* (1938), 305 U.S. 493, 505; *Old Colony Railroad Co.* v. *N.Y., N.H., etc. Railroad Co.*, (2d Cir. 1938) 98 F. 2d 670, 672; *Kuhner* v. *Irving Trust Co.*, (2d Cir. 1936) 85 F. 2d 35, 38; *United Fuel Gas Co.* v. *R.R. Comm.* (1929) 278 U.S. 300, 317-8; *United States* v. *Westinghouse Electric* (1950), 339 U.S. 261, 267.

The *DuBois* case holds that the rate of capitalization, for which the rate of discount was substituted by P.D.C., is dependent upon economic and statistical surveys applicable to the particular enterprise and may not be ascertained by mere reference to formulæ found in textbooks; and such surveys must include studies as to the future rental value of riskless capital plus risk factors.

Yet Mr. Hettinger testified that no attempt was made to ascertain the probable future interest rate by statistical or economic studies (Tr. 390).

What P.D.C. did is not only contrary to the *DuBois* case, but is not borne out by Bonbright or the editions of Badger and Dewing published since the decision in the *Du Bois* case.[10]

4. Confiscatory Character of Method

The undiscounted estimated "stream of earnings" from 1974 to the year 2000 are found on page 10 of the Christman Report (Ex. 28). These figures aggregate $105,192,000. As before stated, the earliest time at which the stockholders could reasonably expect payment was sometime in 1974 because restoration of the non-cans

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[10] Bonbright states that the method used by P.D.C. is applicable only to "enterprises of a short life expectancy such as single-mine ventures" (Vol. I, p. 261).

Badger and Guthman's "Investment Principles and Practices", 3rd Edition (a later version of Badger) criticizes the capitalization rates set out by Badger as erroneous and rejects the ten percent rate for insurance companies (pp. 81, 35).

Dewing's "The Financial Policy of Corporations", 1953 Edition, Vol. 2, p. 1310, says:

> "... No matter how clear and definite the pronouncements of the Supreme Court, bankrupt corporations cannot be reorganized according to stereotyped rules."

would not be completed until that year (Ex. 28, pp. 2, 8; see also Tr. 328). The aggregate earnings of $105,192,000 discounted year by year to the middle of 1974 (actually May 24, 1974), at the 10% compounded rate would be $27,724,000. Now, in order to produce $27,724,000 in the middle of 1974 Old Company would have had to have awarded to it as of December 31, 1948, not the sum of $3,000,000 with simple interest at 2½%, but the sum of $16,928,220 with simple interest at 2½%.

In other words even according to the method of valuation employed by the Price Determination Committee and approved by the Insurance Commissioner, and the California courts, the stockholders should have been allowed $17,000,000 and not $3,000,000.

It is shown below that property may not, consistently with due process, be valued as of the present and payment fixed long in the future (see *post,* pp. 48-49).

5. Valuation not Based on Evidence

As above stated, the majority opinion holds that there was substantial evidence to support the order of the Insurance Commissioner because two members of P.D.C. and its chief actuary testified the plan was fair and equitable and protected the rights of all parties (see note 5, *ante* p. 15).

This holding, of course, ignores the fact that the experts acted on guess-work and did not act on evidence.

It is shown below that a valuation based on guess work does not meet the requirements of due process (See *post,* pp. 46-47)

III

THE PLAN OF MUTUALIZATION (EX. 15)

1. Confiscation of $29,000,000

The conditions precedent to the creation of the obligation of New Company to pay the purchase price and interest in the plan of mutualization are that by some date not later than December 31, 1983, (a) restoration of non-can benefits shall have been completely made, (b) the amount of the purchase price of the stock and interest shall have been accumulated in a special fund, and (c) after the payment of the purchase price of the stock New Company shall have admitted assets in excess of all liabilities in the amount of the sum of 4 percent of admitted assets, plus 25 percent of all premiums on group insurance written on the one-year term basis and on all accident and health insurance, collected during the preceding calendar year.[11]

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[11] The language of the Plan of Mutualization is as follows:

"The price of the shares with interest as defined herein shall be paid when and if all of the following conditions have been met, and not until then:

"1. Restoration is completed.

"2. The funds standing in said Special Surplus Fund, plus the capital and surplus standing in the general corporate accounts, equal or exceed the price of the shares with interest as specified herein.

"3. The financial condition of the Corporation is such that after paying for and cancelling the shares it would still have admitted assets in excess of all its liabilities (both valued on bases held to be satisfactory by a majority of the Voting Trustees appointed and acting pursuant to Section III of this Plan, whose decision shall be final and binding on all interested parties) to the amount of the sum of (a) and (b) as follows: (a) four percent (4%) of all its admitted assets according to the form of annual statement required for life insurance companies by the State of California, if any, or in the absence of

There is no dispute about the effect of these provisions of the Plan.

The evidence is that on the happening of the conditions designated (c), the value of the stock will exceed the purchase price and interest by almost $29,000,000.

The formula referred to in (c) calls for substantially more than the amounts heretofore carried as capital and surplus by New Company.[12]

Mr. McAndless, who was Chairman of the Price Determination Committee, testified that "corporate capital and surplus" (i.e., capital and surplus of departments other than the participating department in which stockholders have no property interest) had reached $11,258,000 by the end of 1948. (Tr. 144) Mr. Christman, Chief Actuary of P.D.C., testified that "corporate capital and surplus" would be increased by $7,260,000 by the time P.D.C. determined that non-can restoration would be completed in 1974 (Tr. 693-4). In other words, by 1974 non-cans would be

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such requirement, according to the form of annual statement then in general use, plus (b) twenty-five percent (25%) of the premiums collected during the preceding calendar year on all Group insurance written on the one-year term basis and on all Accident and Health insurance." (Ex. 15, Sec. II, D; Appx. D, pp. 155a-156a)

[12] As of December 31, 1950, the formula would have required in addition to the sums carried by New Company as capital and surplus, the additional sum of $2,600,331.27; as of December 31, 1951, the additional sum of $3,173,845.73; as of December 31, 1952, the additional sum of $4,186,219.44; and as of December 31, 1953, the additional sum of $4,957,138.32.

These figures are taken from the "Report of Association Examination of Pacific Mutual Life Insurance Company, Los Angeles, California, as of December 31, 1953", page 45.

fully paid, the purchase price and interest together approximating $4,875,000 would be in a special fund, and the capital and surplus would be $18,518,000. The stockholders would of course be entitled to both the $4,875,000 and the $18,518,000, but would receive only the sum first mentioned, thus being defrauded of $18,518,000.

But that is not all.

Mr. McAndless also valued the non-par life insurance in force as of the end of 1948 at $7,824,000, and the accident and health insurance in force as of the same date at $2,500,000 (Tr. 144).

So even assuming the amount of non-par and accident and health insurance in force will not increase one penny between 1948 and 1974, by the time New Company becomes obligated under the Plan to purchase the stock in 1974 the stock will be worth $18,518,000 plus $7,824,000, plus $2,500,000, or a total sum of $28,842,000 more than the purchase price and interest.

Apart from the provisions for acceleration which are dealt with below, if non-cans are restored and the purchase price and interest accumulated at any time prior to 1974, the loss to the stockholders would be the above sum of $28,842,000 less at most the sum of $7,260,000 which Mr. Christman testified would be added to surplus by 1974.

(The value of the stock referred to above does not take into account going concern value of New Company, but takes into account only salvage values. See testimony of Mr. McAndless, Tr. 144).

Messrs. McAndless and Christman were New Company's own witnesses and their testimony stands uncontradicted.

The arbitrary character of the valuation is further emphasized by the allowance of only $250,000 to the stockholders for each year the full restoration of Non-Cans should be made prior to 1974. Mr. Hettinger testified that to his own chagrin, this noble contribution to the Plan of Mutualization was made by his eminent colleague Mr. McAndless. That gentleman testified that interest on the bonus was not allowed until after 1974, because humanly speaking, there was no chance for acceleration of more than a few years, and it would take that time to accumulate the purchase price and interest. (Tr. p. 328) But neither Mr. Hettinger nor Mr. McAndless stated that for each $250,000 bonus the stockholders received they would be deprived of over $2,000,000,—the average annual earnings beginning in 1968 (Ex. 28, p. 9). Mr. McAndless himself testified that if restoration of Non-Cans were accelerated the stockholders would be entitled to "the stream of earnings" for the period of acceleration. (Tr. 155) They would not receive such earnings until after 1974 and perhaps not until 1983. There would therefore be no occasion to discount to December 31, 1948, the earnings for the period of acceleration, and thus reduce the $2,000,000 annual figure to a $250,000 annual figure, which is what was done.

2. Deprivation of Incidents of Ownership

A form of new voting trust agreement is attached as an appendix to the Plan of Mutualization and pro-

vision is made for the execution of the same upon the adoption of the Plan.[13]

The new Trustees are given plenary powers over New Company and, unlike the present Voting Trustees who are under the supervision of the Superior Court for Los Angeles County in which the liquidation proceeding is still pending, are authorized to exercise those powers in their own discretion and their discretion is expressly made unreviewable by any court or tribunal. (Ex. 15. Appx., §§ 6-8)

The new Trustees are also empowered to make themselves self-perpetuating. (Ex. 15, Appx., § 12)

The voting trust agreement names eight persons as Voting Trustees all of whom except two are members of the present board of voting trustees.

The Plan cuts off until after 1983 the right of Old Company, given by the Rehabilitation Agreement, to reclaim the stock of New Company, by advancing the funds necessary to restore non-can benefits; and, in the event of the happening of the conditions and contingencies, cuts off that right absolutely.

The Plan also makes the administration of provisions of the Rehabilitation Agreement, which require New Company to write equal amounts of participating and non-participating life insurance, depend upon the unreviewable discretion of the management and the new trustees. (Ex. 15, Appx., § 8) Inasmuch as the principal asset of the Old Company is its interest in non-participating policies, the management and the new trustees are thus empowered to impair or destroy the

[13] In 1947 the year P.D.C. was appointed, § 11,529.5 was added to the Insurance Code, authorizing creation of a voting trust, in connection with the mutualization of solvent insurers.

most important interest of Old Company in New Company.

The Plan also provides that if the payment of the purchase price of the stock of New Company is not made by 1983, the stock shall be returned to the Liquidator; meanwhile the rehabilitation proceeding, pending since 1936, is held in suspended animation. (Ex. 15; Appx. D, p. 164a)

3. Insuring Control of Management

As above stated, of the eight persons named as Trustees in the new Voting Trust Agreement, all but two are Voting Trustees under the present Voting Trust Agreement. The present Voting Trustees, other than the Liquidator, have had ties of interest with the management of New Company and gave their consent in behalf of the stockholders to the Plan of Mutualization under the provisions of subdivision (b) of § 11526 of the Insurance Code of California without any examination whatever of the Plan of Mutualization (Ex. 21, 22).

The ties of interest between Messrs. Kemp and Call, Chairman of the Board and President of New Company, respectively, (who as officers of Old Company consented to the three void orders under which Old Company was seized by the Insurance Commissioner) and the directors of New Company and the old Voting Trustees are real and substantial.[14]

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[14] An examination of Poor's Register of Directors and Executives, 1953 Edition, and the Annual Statement of New Company for 1952 on file with the insurance departments of 40 states, including California, shows that most of New Company's directors and voting trustees are bound together by interlocking financial and corporate ties. Seven, including Mr. Call, are directors and/or officers of Founders' Insurance Company. Five, including Mr. Call and the

To quote more fully from the majority opinion than we have already quoted:

> "The Commissioner apparently concluded that a Plan of Mutualization which could not be destroyed by future action or non-action of shareholders was necessary as a means of inducing both former and prospective policyholders to deal with the New Company and thus permit its continued existence." (Appx. A, p. 12a)

There is no evidence in the record that policyholders refused or would refuse to cooperate with the Insurance Commissioner unless he violated his trust obligations to the shareholders. The established facts are that the purpose of the Insurance Commissioner was to put the reorganizers, who, as officers of Old Company, consented to the three void orders, in control of New Company at the time it was organized[15] and maintain them in control as long as they lived.[16]

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son of a voting trustee, are directors and/or officers of the California Bank. Five, including Mr. Call, and the brother of a voting trustee, are trustees and/or officers of the University of Southern California. In at least ten other corporations two or more directors or voting trustees serve as directors and/or officers. In nine of the corporations referred or alluded to a director or voting trustee of New Company serves as President, Chairman of the Board of Directors, or President of the Board of Trustees, or Executive Vice-President. One or more directors or voting trustees of New Company serve as directors and/or officers of seven banks in which New Company has deposits, and of twelve corporations in which New Company owns securities. Such deposits and security holdings are substantial.

[15] See Transcript of appeal in *Carpenter* v. *Pacific Mutual, supra,* a part of the record in *Neblett* v. *Pacific Mutual, supra,* pp. 12, 234, 579-581, 150, 57, 95, 315, 713, 801. See *United States* v. *Pink,* (1942) 315 U.S. 203.

[16] The transfer of the stock to voting trustees was designed to accomplish that end.

Mr. McAndless was unable to point out any benefits to the policyholders from mutualization (Tr. 235, 236, 240).[17]

This is not surprising as when policies are properly reserved, policyholders are not benefited by piling up huge surpluses or adding a tremendous volume of additional business. The benefits in such cases are to the management. Thus, the old Equitable, which was a stock company, had a surplus of $80,000,000 and about $1,500,000,000 of insurance in force; and the controlling stock, on which the dividends were limited to $3,500.00 annually, sold for $4,000,000. See *Royal Trust Co.* v. *Equitable Life Assurance Society,* 2d Cir. (1917) 247 Fed. 437.

Mr. Spain, who was counsel of New Company's General Agents' Association, admitted that the whole purpose of mutualization was to insure continued corporate control by the management (Tr. 1122, 1123, 1125-6, 1130-2).

For forty years no significant conversion from a stock company to a mutual company has occurred except where the management's control of the stock company was jeopardized. This was the case in both the Metropolitan and Prudential mutualizations. As early as 1913 the Pujo Committee declared "that the so-called control of life insurance companies by policyholders through mutualization is a farce and its only result is to keep in office a self-constituted and self-

[17] It is claimed that mutualization is for the benefit of the life policyholders. Yet the life policyholders have not appeared in this proceeding. The Plan of Mutualization has been sponsored by New Company, not the life policyholders (Tr. 674-5).

perpetuating management which can usually rely on the agency force to more than offset any policyholders' uprising if such a thing is conceivable." (Report, pp. 146-147). The conclusion of the Pujo Committee is borne out by a report made in 1941 by the Securities and Exchange Commission to the Temporary National Economic Committee (T.N.E.C. Monograph #28, pp. 64-87). (See particularly, Hearings of February 1939, Part IV, Ex. 258, pp. 1555-1557)

IV

The Compulsion Resulted from the Order of the Insurance Commissioner

The majority opinion says:

> "The approval of the mutualization plan by the Commissioner did not involve any deprivation of property rights or vested rights; it was in essence a permit or license authorizing the New Company to purchase its own stock." (Appx. A, p. 13a)

This conclusion is based on the assumption that the compulsion upon appellants to sell arose from the Rehabilitation Agreement and not the order of the Insurance Commissioner.

The record affirmatively shows this assumption is utterly without foundation.[18]

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[18] In cases involving due process, "The basis in Fact upon which the State Court rested its decision" will be reviewed by this Court to determine whether it "has any support in the record" (*Postal etc. Co.* v. *Newport* (1917) 247 U.S. 464, 473; *Fayerweather* v. *Ritch* (1904) 195 U.S. 276, 297-9; *Carlson* v. *Washington* (1913) 234 U.S. 103, 106; *Hansberry* v. *Lee* (1940) 311 U.S. 32).

1. The Rehabilitation Agreement Was, at Most Binding on the Liquidator

The Rehabilitation Agreement provides that if the report of P.D.C. is that mutualization is "then practicable" and if New Company is requested by policyholders to submit the Plan of Mutualization reported by P.D.C. "in accordance with the laws of the state of California then in force":

> *"New Company will promptly submit the same* [i.e., proposed plan] *in accordance with the laws of the State of California then in effect."* (Ex. 9, par. 20(a); Appx. D, p. 148a)

The Rehabilitation Agreement further provides:

(a) "The *Conservator,* for himself, and for any successors in the ownership of said stock * * * agrees to consent and hereby *consents as the holder and owner of the stock* of New Company to *such plan of mutualization."*[19]

(b) *"In the event said mutualization plan is adopted, the Conservator,* or a Liquidator as aforesaid, *shall dispose of such stock in accordance with such plan."* (Ex. 9, par. 20(a); (Appx. D, p. 148a).[20]

The stipulations in the Rehabilitation Agreement, according to its very language, are by the Commis-

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[19] In 1936, when the Rehabilitation Agreement was executed, § 11,526(b) required approval of shareholders to be by vote at a special meeting of shareholders called for that purpose. In 1937 the subsection was amended to also authorize approval by written consent of the shareholders.

[20] The Insurance Commissioner conceded in the state supreme court that the consent given in the Rehabilitation Agreement by

No compulsion, therefore, resulted from the Rehabilitation Agreement. The compulsion did result from the order of the Insurance Commissioner.[21]

4. The Plan of Mutualization Expressly Requires the Transfer of the Stock in the New Voting Trustees

The Plan of Mutualization expressly requires the present voting trustees to transfer the stock to the new voting trustees as soon as the Plan is adopted, viz., approved by the Commissioner and the policyholders and filed. (Appx. C, pp. 157a-158a)

5. The Order of December 4, 1936 is Part of the Totality of State Action

As stated above, under the statute the Conservator had no power to execute a rehabilitation agreement except pursuant to court order. If it should be held, therefore, that compulsion on the stockholders did not flow from the order of the Insurance Commissioner alone, then for purposes of due process, according to the authorities, this Court should, we submit, consider the totality of state action including the order of December 4, 1936. (*Wheeling Steel Corp.* v.

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[21] In *In re Vulcan & Reiter Co.*, 2d Cir. (1947), 152 F. 2d 92 at page 93, it is said:

> "For the purposes of the composition all creditors are treated as a class, and the will of the majority is enforced upon the minority, provided the decision of the majority is approved by the Court. *Except for this coercion of the minority, the intervention of the court of bankruptcy would hardly be necessary!*"

In 41 *Am. Jur.*, pages 823-824, it is said:

> "A power to sell, either in a will or deed, to be exercised on the happening of a particular event, cannot by law be exercised until the happening of that event, in fact, the power does not exist until then."

Glander, (1949) 337 U.S. 562, 570; *Cole* v. *Arkansas,* (1948) 333 U.S. 196, 201; *Frank* v. *Mangum,* (1915) 237 U.S. 309, 327-8).

RAISING OF THE QUESTIONS BELOW

Appellants have maintained throughout this proceeding both in the trial and appellate courts, that the order of the Insurance Commissioner approving the Plan of Mutualization and the application of §§ 11,526 and 11,527 of the Insurance Code of California as construed and applied in this case, deprive them of their property without due process of law, contrary to amendment XIV of the Constitution of the United States.

The questions were raised in the California appellate courts by Appellants' briefs and petitions filed in said Courts. (R. Fold, 3, App. Open. Br. pp. 75-175, 187-90, 238-43, 230-2; Pet. For Hear. pp. 71-97)[22]

The opinions of those courts clearly indicate that the questions were there passed upon.

The majority opinion in the state supreme court rejected most of appellants' due process contentions by holding that:

> "The approval of the Mutualization Plan by the Commissioner did not involve any deprivation of property rights or vested rights; it was in essence a permit or license authorizing the new company to purchase its own stock. Under these circumstances, the function of the superior court was to determine whether the action taken by the commissioner was arbitrary or constituted an abuse of discretion and in upholding the action of the com-

[22] The California Rules of Court on Appeal provide that briefs filed in the District Court of Appeal become briefs in the California Supreme Court upon the granting of a hearing by the latter court.

missioner, it properly refused to conduct a trial de novo [i.e., weigh the evidence in the record and exercise its own independent judgment]." (Appx. A, p. 13a)

That majority opinion further states:

> "Plaintiffs' contention that there was a denial of procedural due process is based on their claim that the commissioner accepted the conclusions of the price determination committee without having before him all the facts on which these conclusions were based, and that the committee itself relied on statistics furnished by its actuary without reviewing all the supporting data." (Appx. A, p. 14a)

That contention was likewise rejected on the ground that appellants could have requested further information from the members of PDC who testified at the hearing before the Commissioner (Appx. A, p. 14a)

The opinion also holds:

> "Plaintiffs nevertheless contend that it was improper to follow the procedure set up in the code for mutualization of a solvent company, because, they assert the commissioner in doing so, was forced to act in a dual capacity with conflicting interests.... In numerous cases where the action of an administrative officer was necessary to prevent defeat of the statutory scheme, his participation has been upheld, although the grounds for disqualification were much more serious than those raised here." (Appx. A, pp. 6a-7a)

The following quotations are from the dissenting opinion of Carter, J. in the state supreme court:

> "In approving this transaction, the majority disregards express statutory provisions of this state

and deprives the stockholders and policyholders of old company of their right to a judicial review of the administrative proceeding whereby they were deprived of their property, thus denying them due process of law to which they were entitled under both state and federal constitutional provisions". (Appx. A, p. 19a)

"I have heretofore set forth at length the self-evident fact that appellants are possessed of vested property rights, of which they are being deprived." (Appx. A, p. 56a)

"Appellants here complain bitterly because the mutualization plan provides that the price to be paid for New Company stock (of which they are the *beneficial owners*) is $3,000,000. . . . It surely must be crystal clear to everyone who can think that such an outrageous confiscation of property has never before taken place in this state." (Appx. A, p. 57a)

"The only rational conclusion to be drawn from the facts of this case is that appellants were deprived of a vested property right and, therefore, should have been given a trial de novo in a *judicial tribunal* provided by the State for the protection of private property rights. Because appellants were not afforded a trial de novo, they have been deprived of their property without the due process of law guaranteed to them by both the state and federal constitutions." (Appx. A, pp. 58a-59a)

The questions here involved were likewise passed upon by the District Court of Appeal. That Court said:

"Another point raised by the appellants is that they have been deprived of substantive due process because the stock of the New Company was valued as of the present, that the time of payment was fixed long in the future, payment was conditional,

there was no provision for reasonable interest, and the price paid was grossly inadequate. On this question of due process we should never lose sight of the fact that the commissioner's approval of the Plan of Mutualization did not have the effect of taking appellants' property, since it was nothing more or less than a permit. . . ." (Appx. B, p. 91a)

The questions were initially raised by Appellants in their Petition for Mandate filed November 9, 1950, in the Superior Court.

Paragraph XXII of that petition alleged that said order of the Insurance Commissioner, dated September 22, 1950, was arbitrary and unreasonable; that its issue constituted an abuse of discretion by the Insurance Commissioner; that findings contained therein were clearly erroneous, contrary to the evidence, and not supported by substantial evidence adduced at the hearing, or otherwise; and that:

> "said Findings and Order of said Commissioner deprive petitioners, and each of them, of property without due process of law, contrary to the provisions of the Constitution of the State of California and the Fourteenth Amendment to the Constitution of the United States. In this respect, Petitioners here refer to their Points of Error hereto attached and presented with this petition." (Clk. Tr. 22)

The Points of Error attached to the Petition for Mandate allege that the Plan contains no unconditional promise on the part of New Company to pay the fair value of the stock of New Company; that no valid consent to the Plan of Mutualization on behalf of Old Company, the beneficial owner of the shares, as

required by § 11,526 of the Insurance Code, was ever given; that said §§ 11,526 and 11,527 do not apply to an insurer whose stock is owned or voted by the Insurance Commissioner or by Voting Trustees acting on his behalf, nor to an insurer where the Commissioner is required to consider a Plan of Mutualization in some capacity other than his official capacity as Commissioner; that the Plan of Mutualization is in fact a thirty-three year option depriving the Old Company of its right to repossess the stock by paying the full amount required to restore non-can benefits; that the stock was valued by guesswork and uncertain criteria contrary to law; that the members of the Price Determination Committee were not impartial or disinterested; and that the Insurance Commissioner was required independently to determine the value of the stock before approving the Plan. (Clk. Tr. 28-36)

Paragraph XIII of said petition further alleges that Old Company has a beneficial interest in the stock of New Company, with a value in excess of $7,500,000 which in eight years would have a value in excess of $25,000,000. (Clk. Tr. 13)

The Superior Court decided contrary to appellants' contentions, holding that §§ 11,526 and 11,527 applied and were not objectionable; that the Commissioner's duty was merely to determine if PDC had acted arbitrarily; and that PDC had not acted arbitrarily. (Appx. C, pp. 115a-116a, 121a-123a)

The due process contentions of appellants heretofore mentioned were further maintained by them in their petition for rehearing filed in the State Supreme Court. (pp. 23-42, 10, 7; in R. Fold. 3)

THE CASE IS WITHIN THE JURISDICTIONAL PROVISIONS RELIED ON

I

A Proper Case for Appeal Is Presented Because the Order of the Insurance Commissioner Is Legislative in Character

Mutualization of an insurance company is a legislative function, an exercise of the reserved power of the legislature to alter, amend and repeal corporate charters. The order of the Insurance Commissioner approving the Plan of Mutualization here involved was therefore legislative in character. *Lord* v. *Equitable Life Asssurance Society,* (1909) 194 N. Y. 212. While, to perform his delegated function to pass on the fairness of the Plan, the Commissioner had to act quasi-judicially, his order had a legislative effect and was a legislative act. *Belden* v. *Union Central Life Insurance Co.,* (1944) 143 Ohio St. 329; *In re Prudential Insurance Company of America,* (1913) 82 N. J. Eq. 335; *Rippel* v. *Prudential Insurance Company of America,* (1914) 85 N. J. L. 395; *Application of Prudential Insurance Company of America,* (1942) 132 N. J. Eq. 170.

The stockholders in an insurance company have a vested right to retain their stock or sell it at their own price. This vested right cannot be taken away from them by the legislature under its reserved power to repeal, alter or amend corporate charters. *Lord* v. *Equitable, supra.* Compulsory mutualization differs from merger. In merger cases dissenting stockholders can be forced to sell because they are given an option to become stockholders in the merged corporation or sell their stock at an appraised price. (See *Breslav* v. *Light and Power Co.,* (1936) 249 App. Div. 181, (affirmed (1937) 273 N. Y. 593), *Wheatley* v. *Root,* (1946) 147 Ohio St. 127, *Yukon* v. *Vose,* (1949) 201

Okla., 376, 379.) There is obviously no such option in cases of compulsory mutualization.

The situation here is aggravated because the Conservator and management, by manipulations carried out under the forms of law, undertook to require the stockholders to sell their stock at a price fixed by persons with ties of interest with the management. (See *Mason* v. *Pewabic Mining Co.,* (1890) 133 U.S. 50; *Breslav* v. *Light and Power Co., supra.*)

The other points decided by the state supreme court showing that this is a proper case for appeal on the grounds above stated appear from the *Statement,* and are specifically referred to under the heading: "The questions are so Substantial as to Require Plenary Consideration."

II

A Proper Case for Appeal Is Presented Because the Validity Under the United States Constitution of State Statutes, as Construed and Applied by the State Court, Is Involved

§§ 11526 and 11527 of the Insurance Code of California, as construed and applied in this case, required appellants to sell their stock without their consent in return for a price fixed in the Plan of Mutualization, formulated by P.D.C. as a result of secret investigations of which no record was kept; approved by the Insurance Commissioner after reviewing the action of P.D.C. only to determine whether P.D.C. had acted arbitrarily and not to determine whether, in the independent judgment of the Insurance Commissioner, the Plan was fair and equitable; and judicially reviewed only to determine whether the Insurance Commissioner, in approving the Plan, had acted arbitrarily or abused his discretion and not to determine

whether, in the independent judgment of the courts the Plan was fair and equitable.

§§ 11526-11527, as construed and applied in this case, required appellants to submit to the before mentioned procedure even though two of the four members of the P.D.C. had ties of interest with the management of New Company; the Insurance Commissioner reviewed only a small fraction of the data considered by P.D.C.; and the Insurance Commissioner at the time he approved the Plan had conflicting interests and duties, which precluded his acting impartially.

P.D.C., composed of four private persons, was authorized by the Rehabilitation Agreement, not only to value the stock but to determine sometime after 1946 whether mutualization was "then practicable", to fix the terms of payment, to formulate an elaborate plan of mutualization, and to prepare an elaborate trust instrument and name self-perpetuating trustees. In short, P.D.C. was given the combined powers exercised by a district judge and securityholders' committees in a reorganization proceeding. This delegation of legislative and quasi-judicial powers to P.D.C. was violative of due process. (See *Fink* v. *Cole*, (1951), 302 N. Y. 216, holding, on the authority of the decisions of this Court, that a statute empowering the Jockey Club of New York to license race tracks is unconstitutional.)

The Insurance Commissioner violated due process also because he did not exercise his own discretion. (See *U.S. ex rel Accardi* v. *Shaugnessy* (1954), 347 U.S. 260; S.C. on later appeal (1955) 99 L. Ed. Adv. 637.)

Inasmuch as the decision here was virtually that of P.D.C. and not of the Insurance Commissioner, we

submit the appellants were entitled, under the United States Constitution, to full judicial review by the California courts. (See *St. Joseph Stockyards Co.* v. *U.S.* (1936) 298 U.S. 38; *Ohio Valley Water Co.* v. *Ben Avon Borough* (1920) 253 U.S. 287; *United Railways Co.* v. *West,* (1930) 280 U.S. 234. See also dissenting opinion of Carter, J. (Appx. A, pp. 55a-56a)

The state supreme court held that the Insurance Commissioner acted as a judge in his own case,[23] but that his order was not thereby vitiated because of the doctrine of necessity. (Appx. A, pp. 6a-7a) Any necessity there may have been, however, was due to a misapprehension as to due process. Under § 1094.5 of the California Code of Civil Procedure (Appx. F, pp. 185a-186a) and *Thomas* v. *Cal. Emp. Com.,* (1952) 39 Cal. 2d 501, the California courts, where a property right is involved, must weigh the evidence. If they had done so here, the case would have been reversed, as stated by the trial judge himself. (Appx. A, p. 58a) Here appellants have vested property rights under the Federal Constitution (*Ante,* pp. 42, 32, note 18). Any necessity was also due to the misapprehension that the

[23] It may be noted that although Old Company was made a party to the proceeding before the Insurance Commissioner, the Liquidator (who, be it repeated, was trustee for the Old Company) did not represent or undertake to represent Old Company. Moreover the Liquidator was named a respondent in the petition for mandate only because, after demand, he refused to bring a proceeding to review his order as Commissioner (Clk. Tr. 4). In addition, although as Commissioner he is only a formal party and as Liquidator only a nominal party, the Commissioner in both capacities has, by counsel, opposed his *cestui que trustent* at every step in the litigation. (See *Appeal of Cabot Bank,* (1857) 26 Conn. 7) It is worthy of note that the life policyholders, for whose benefit the mutualization is supposed to be, have not appeared at a single stage of the mutualization proceedings.

order of the Insurance Commissioner was not compulsory. This misapprehension has no basis whatever in fact and so is subject to review by this Court. See *Hansberry* v. *Lee,* (1943) 311 U.S. 32.

It is clear, therefore, that §§ 11526-7 as construed and applied in this case were violative of procedural due process.

Consent given to unconstitutional procedures is not binding on anyone. (*Terral* v. *Burke Construction Co.,* (1922) 257 U.S. 529; *Hanover Fire Insurance Co.* v. *Harding,* (1926) 272 U.S. 494; *Fidelity and Deposit Co.* v. *Tafoya,* (1926) 270 U.S. 426.

The advance statutory consent given or purported to have been given by the Conservator as trustee for the stockholders to any plan of mutualization which a price determination committee later might promulgate was, therefore, ineffectual.

THE QUESTIONS ARE SO SUBSTANTIAL AS TO REQUIRE PLENARY CONSIDERATION

I

Valuation by Speculation

The valuation of a going business whether it be an insurance company, a bank, a railroad or an industrial corporation, cannot be left to chance or guess-work. Since the decision of this Court in the leading case of *Consolidated Rock Products Company* v. *Du Bois,* (1941) 312 U.S. 510, the law of valuation has been largely rewritten by the courts. In the absence of an actual market or where market value is not the appropriate criterion (both of which conditions were present here), substantially the same criteria have been applied by the courts under various designations, i.e., "in-

vestment value", "fair market value", "fair cash value", "true cash value". These criteria have been applied in reorganization cases involving the issuance of new securities, simplification proceedings involving the retirement of a class or classes of stock, appraisals for tax purposes and the retirement of stock of stockholders dissenting from mergers. In practice there are few more difficult questions in the realm of law, accounting, or tax administration. Many points are still unsettled but it is settled that property may not be valued, consistently with due process, on the basis of guess-work or assumptions having no rational basis in fact or by reference to mere formulæ, as was done here (*West Ohio Gas Co.* v. *Public Utilities Commission,* (1935) 294 U.S. 79; *Northern Pacific Railway Co.* v. *Department of Public Works,* (1925) 268 U.S. 39); and that determination of a "fair rate of return" (which presents substantially the same problems as the determination of the discount rate here) without any factual basis and on the basis of Commission expertise alone is arbitrary action. (*Washington Gas Light Co.* v. *Baker,* (D.C. Cir. 1950), 188 F. 2d 11 (cert. den.); *Capital Transit Co.* v. *Public Utilities Commission,* (D.C. Cir. 1953), 213 F. 2d 176 (cert. den.)) The authority of these cases, which the state supreme court ignored, would be weakened if the decision of the state supreme court were not reviewed by this Court on the merits; and serious confusion would result among lawyers, judges, accountants, tax officials and others concerned in practice with the valuation of innumerable classes of property.

II

Valuation as of Present and Payment in Distant Future

It has long been held in condemnation cases that properly cannot, consistently with due process, be valued as of the present with provision for payment in the distant future, either because the values might differ (*Bensley* v. *Mountain Lake Water Co.,* (1859) 13 Cal. 306; cf. *Benedict* v. *City of New York* (2nd Cir. 1899) 98 Fed. 789); or merely because of the delay in payment. *Butler* v. *Sewer Commissioners,* (1877) 39 N.J.L. 665; *Waterbury* v. *The Platt Brothers and Company,* (1904) 76 Conn. 435; *McGibson* v. *Roane County Court,* (1924) 95 W. Va. 338; see also *United States* v. *Westinghouse Electric & Mfg. Co.,* (1950) 339 U.S. 261). The principle applied in the cases cited has also been applied in reorganization cases. (*In re Murel Holding Corp.,* (2d Cir. 1935) 75 F. 2d 941; *Provident Mutual Life Insurance Co.* v. *University Evangelical Lutheran Church,* (9th Cir. 1937) 90 F. 2d 992).

In *S.E.C.* v. *Central Illinois Securities Corp. et al.,* (1949) 338 U.S. 96, in passing on the fairness and equity of a plan to simplify a stock structure by retiring securities, this Court said:

> "Valuation . . . necessarily has primary relationship to value as of the time the stockholders' surrender becomes effective, not as of some earlier remote period or one long afterwards." (p. 139)

It is important to the administration of justice in mutualization and reorganization cases and in valuation matters generally, both litigated and unlitigated, that the above dictum of this Court be made a matter of decision and put upon a constitutional basis. This

is particularly true where it affirmatively appears, as it does in this case, that there is a wide diversity between the value of the property at the time at which value is fixed and at the time when the amount fixed is payable, particularly where reasonable interest is not provided for and the corporation is placed in the control of persons hostile to the stockholders without any security being given to the stockholders. (*Louisville Joint Stock Land Bank* v. *Radford,* (1935) 295 U.S. 555)

III

Deprivation of Incidents of Ownership for 35 Years

The order of December 4, 1936, approving the Rehabilitation Agreement, by providing that the Conservator or a Liquidator, if appointed, could not dispose of the stock, except subject to the procedures for mutualization provided for in the Rehabilitation Agreement, virtually imposed a moratorium that has already lasted 19 years. This moratorium rendered useless the provisions in the Rehabilitation Agreement authorizing Old Company to acquire the stock of New Company by fully restoring Non-Can benefits. Manifestly, no one would put up $20,000,000, more or less, to acquire the stock of Old Company, and hazard getting only $3,000,000 back on mutualization.

The Plan of Mutualization extends the moratorium another 35 years; only if mutualization fails in 1983 is the stock to be returned to the Liquidator as trustee for Old Company.

Meanwhile, New Company is in the hands of hostile voting trustees and directors who are expressly given power, in their uncontrolled discretion, to do acts, which if done, will ruin Old Company's investment.

The Plan of mutualization, therefore, deprives Old Company of the incidents of ownership contrary to due process. (*Louisville Joint Stock Land Bank* v. *Radford, supra; Old Dearborn Distributing Co.* v. *Seagram-Distillers Corp.*, (1936) 299 U.S. 183).

If the decision of the state supreme court is not reviewed by this Court on the merits, turnpike promoters could subject real property to options to purchase for 50 years at the land's present value; municipalities could impose similar options on suburban areas; others having the power of eminent domain, whether governmental or private agencies, could impose similar options on potential oil or mineral lands and thus engage in long term speculations solely at the risk of the property owners.

IV

Secs. 11526-7 as Construed

It is shown in the next preceding section that §§ 11526-7 as construed and applied in this case violate procedural due process. We know of no reported case in the field of administrative practice, where the violations of due process have been more numerous or more flagrant. If the decision of the state supreme court is permitted to stand, without review on the merits by this Court, there is, we maintain, clear and present danger that administrative bodies generally will be encouraged to engage in high-handed unconstitutional practices. We also maintain that the administration of the insurance laws of many states will be thrown into confusion because §§ 11526-7 of the California Insurance Code were copied from the New York

statute, and the New York statute has been copied with only formal changes in at least twelve other States.[24]

V

Mutualization as a Device for Corporate Control

One of the most baffling problems in corporate practice is the control of corporations by self-perpetuating groups with practically no beneficial interest. As stated by Dr. Paul A. Samuelson, Professor of Economics at M.I.T., in his book, "Economics", 1948:

> "Berle and Means, in a path-breaking study point out that this wide diversification of stockholding has resulted in a *separation of ownership and control.* Recent events have confirmed the fact that in the typical giant corporation, all management together—officers and directors—hold only about 3% of the outstanding common stock. The largest single majority ownership groups typically hold only about one-fifth of all outstanding voting stock. Such a small fraction is considered more than enough to maintain 'working control'." (p. 128)

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[24] District of Columbia (*Dist. of Columbia Code, 1951 ed, Title 35, § 35-519*); Illinois (*Smith-Hurd Annotated Statutes, Chapter 73, § 647*); Minnesota (*6 Minnesota Statutes Annotated, Chapter 61, §§ 61.461 and 61.462*); New Jersey (*New Jersey Statutes Annotated, 17:34-33 to 34-43.7*); New York (*Book 27, part 2, McKinney's Consolidated Laws of New York § 199*); Ohio (*Page's Ohio Revised Code, Annotated, §§ 3913.01 to 3913.10*); Oregon (*7 Ore. Compiled Laws, Ann., §§ 101-601 to 101-611*); Pennsylvania (*Purdon's Penn. Statutes, Ann., Title 40, §§ 592 to 595*); South Dakota (*1952 Supplement to South Dakota Code of 1939, §§ 31.1803 to 31.1806*); Tennessee (*4 Williams Tennesee Code Annotated (1934), 1952 Pocket Supplement, §§ 6433.14 to 6433.31*); Texas (*14 Vernon's Texas Civil Statutes, Article 21.27*) Utah (*4 Utah Code Annotated (1953) § 31-8-7*); Virginia (*6 Code of Va., 1950 §§ 38.1-489 to 38.1-495.5*).

> "This suggests that *the future problem* may not be one of choosing between large monopolistic corporations and small scale competitors but rather that of *devising ways to improve the social and economic performance of large corporate aggregates.*" (p. 132)

Since this passage was written the problem has become exigent because of proxy fights made possible by SEC rules governing proxy statements, and as a result of Congressional investigations. Inasmuch as (according to the testimony of Mr. Carroll M. Shanks, President of the Prudential Insurance Company of America, on November 30, 1949, before the House Subcommittee on the Study of Monopoly Power) the management of mutual companies is necessarily self-perpetuating, it is, we maintain, in the highest public interest that mutualization should not be permitted to be used as a device for corporate control except in strict accordance with constitutional modes established by this Court.

VI

Other Substantial Questions

The constitutionality of compulsory mutualization has not been decided by this Court, and this Court has not heretofore determined in a civil case that due process depends upon the totality of state action.

These, we submit, are important questions which require plenary consideration.

The decision of the California Supreme Court that the mutualization was voluntary (and therefore the order of the Insurance Commissioner did not deprive appellants of a vested right but merely constituted a permit to New Company to buy its stock) deprives ap-

pellants of due process. As pointed out by Carter, J. (Appx. A, p. 22a) this mutualization is as voluntary as a confession beaten out of a helpless prisoner. The question thus presented is important and, we submit, requires plenary consideration.

A decision on the merits by this Court would not only redress great private wrongs, which will otherwise result in despoiling appellants of nearly $30,000,000, but would also aid in the administration of public justice by showing that similar outrages will not be permitted in violation of due process "while this Court sits."

ALTERNATIVE APPLICATION FOR CERTIORARI

In the event this Court should hold that this is not a proper case for appeal, we respectfully ask that this Jurisdictional Statement be treated as a Petition for Certiorari, and that this Court issue its writ directed to the Supreme Court of California to the end that the case may be reviewed on the merits by this Court.

It is submitted that the courts below decided erroneously questions of general importance which this Court should herein determine on Appeal or Certiorari.

Respectfully submitted,

JOSEPH L. LEWINSON
HENRY W. LOW
Attorneys for Appellants

FRANK E. HOLMAN
Of Counsel

December 21, 1955

APPENDIX

APPENDIX A.

Opinions in the Supreme Court of California

[L. A. No. 23261. In Bank. June 27, 1955.]

THE PACIFIC MUTUAL LIFE INSURANCE COMPANY OF CALIFORNIA (a Corporation) et al., Appellants, v. F. BRITTON McCONNELL, as Insurance Commissioner, etc., et al., Respondents.

* * * * * * * * * *

APPEAL from a judgment of the Superior Court of Los Angeles County. Paul Nourse, Judge. Affirmed.

Proceeding in mandamus to review action of Insurance Commissioner in approving plan for mutualization of an insurance company. Judgment denying writ affirmed.

Joseph L. Lewinson, Frank B. Belcher, C. Ray Robinson, Henry W. Low and William B. Boone for Appellants.

C. Ray Robinson and William B. Boone, as Amici Curiae on behalf of Appellants.

O'Melveny & Myers, Paul Fussell, Homer I. Mitchell, James E. Cross, George B. Gose, Frank P. Doherty, Guy Knupp and Peery Price for Respondents.

Lloyd W. Dinkelspiel and Heller, Ehrman, White & McAuliffe, as Amici Curiae on behalf of Respondents.

GIBSON, C. J.—The Pacific Mutual Life Insurance Company of California (hereinafter referred to as the "old company") and certain of its stockholders brought this mandamus proceeding in the superior court to review the action of the Insurance Commissioner in approving a plan for mutualization of a second corporation, Pacific Mutual Life Insurance Company (hereinafter called the "new company"), which had been organized by the commissioner as part of the rehabilitation of the old company. The court upheld the action of the commissioner, and plaintiffs have appealed from the judgment.

In 1936 the old company was in a hazardous and insolvent condition within the meaning of the Insurance Code, and its business and assets were taken over by the Insur-

ance Commissioner,* as authorized by statute. (Ins. Code, §§ 1011, 1013.) Pursuant to section 1043 of the code, a rehabilitation agreement was entered into between the new company and Commissioner Carpenter, as conservator of the old company, whereby most of its assets were transferred to the new company in exchange for all the new company's capital stock. The stock was to be held by the commissioner as conservator for the benefit of the creditors, policyholders and stockholders of the old company. The new company assumed substantially all the obligations of the old company, including a limited obligation with respect to noncancellable accident and health policies (referred to herein as "non-can policies"), and agreed to set up a special fund for restoration of benefits to holders of those policies.

In December, 1936, after a hearing, the superior court approved the rehabilitation agreement and authorized the commissioner to perform all the obligations required on his part. This order was affirmed in *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal.2d 307 [74 P.2d 761]. (Affd. in *Neblett* v. *Carpenter*, 305 U.S. 297 [59 S.Ct 170, 83 L.Ed 182].) In February, 1937, an order was made providing for the liquidation of the old company and appointing the commissioner as liquidator. It was upheld in *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 13 Cal.2d 306 [89 P.2d 637]. In 1938 the commissioner transferred the stock of the new company to five trustees who were given legal title to the stock with power to vote it in accordance with the purposes of the rehabilitation agreement. The order approving the transfer was affirmed in *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 344 [139 P.2d 908].

The rehabilitation agreement set forth the method by which a plan for mutualization of the new company could be formulated. It provided that 10 per cent of the participating life policyholders could request the new company to create an appointing committee consisting of the presi-

* Six successive commissioners, Messrs. Carpenter, Goodcell, Caminetti, Garrison, Downey and Maloney, have passed upon matters relating to the insolvency of the old company.

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dent of the Life Insurance Association of America, the president of Stanford University and the provost of the University of California at Los Angeles. The appointing committee was directed to select a price determination committee composed of persons skilled in matters of insurance company valuation. If the price determination committee concluded that voluntary mutualization could be practicably accomplished, it was to propose a plan of mutualization in accordance with the laws of this state. By the terms of the agreement the commissioner, as sole shareholder of the new company, consented in advance to the plan of mutualization to be formulated.

A price determination committee was appointed, consisting of Alva J. McAndless, president of the Lincoln National Life Insurance Company of Fort Wayne, Indiana; Horace R. Bassford, vice president and chief actuary of the Metropolitan Life Insurance Company of New York; Ray D. Murphy, vice president and chief actuary of the Equitable Life Assurance Society of New York; and Albert J. Hettinger, a partner in Lazard Freres and Company, a firm engaged in investment banking. After three years of study the committee proposed a plan of mutualization, which provides that, upon the occurrence of certain conditions, the new company shall buy all of its own capital stock for $3,000,000, plus interest from December 31, 1948, the price to be augmented should the restoration of benefits under the non-can policies be completed before 1973.

The proposed plan of mutualization was adopted by the directors of the new company on May 5, 1950. On September 22, 1950, after a hearing, Commissioner Downey approved the plan, finding that it would be fair and equitable in its operation, and thereafter it was approved by the policyholders of the new company. This proceeding in mandamus was then brought to review the action of the commissioner, and the trial court concluded that there was substantial evidence to support his findings and that he had not exceeded his jurisdiction or abused his discretion in approving the plan.

Plaintiff attacks the judgment upon numerous grounds, and, although many of their contentions may be disposed of

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by application of principles of res judicata, we believe that the problems may be more clearly presented by first discussing the propriety of the determination of the various points without regard to the binding effect of prior adjudications.

The first problem which we must consider is whether the proper statutes were followed in the formulation and approval of the mutualization plan. As contemplated by the rehabilitation agreement, all steps in connection with the adoption of the plan were taken pursuant to section 11525 et seq. of the Insurance Code, which relate to voluntary mutualization of a solvent insurer.* Plaintiffs assert that the applicable statutes for mutualization of the new company are sections 1043 et seq., which govern involuntary mutualization of an insolvent insurer.† [1] The essential

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* Section 11525 of the Insurance Code provides: "A solvent domestic incorporated insurer having a paid-in capital represented by outstanding shares of capital stock and issuing, on a reserve basis, nonassessable policies of life insurance or of both life and disability insurance, may convert itself into an incorporated mutual life insurer, or life and disability insurer, issuing nonassessable policies on a reserve basis. To that end it may provide and carry out a plan for the acquisition of the outstanding shares of its capital stock for the benefit of its policyholders, or any class or classes of its policyholders, by complying with the requirements of this chapter."

Sections 11526-11533 contain detailed provisions relating to procedure for adoption and execution of the plan of mutualization.

† Section 1043 of the Insurance Code provides in part: "In any proceeding under this article, the commissioner, as conservator or as liquidator, may, subject to the approval of said court, and subject to such liens as may be necessary mutualize or reinsure the business of such person, or enter into rehabilitation agreements." The words "such person" include an insolvent insurer as referred to in sections 1010 et seq. of the Insurance Code dealing with insolvency and delinquency.

Section 1045 provides: "If at any time after the issuance of an order under section 1011 . . . it shall appear to the commissioner that the purposes of section 1011 can be best attained by the mutualization of such life insurer, the commissioner may formulate a plan for mutualization of such insurer." Section 1046 et seq. set forth the necessary procedural steps.

DARK PAG

differences in procedure are that under the sections relating to voluntary mutualization of a solvent company the plan is adopted by the directors, subject to approval by the stockholders and the commissioner, and no court proceedings are necessary; whereas under the provisions for involuntary mutualization of a seized insurer the plan is formulated by the commissioner as conservator without consent of the stockholders or directors, and it must be approved by the court.

[2a] The new company is solvent and nondelinquent, and there is no sound reason why it should be mutualized under the statutes relating to insolvent insurers. [3] The commissioner had power to create the new corporation in order to preserve the business of the seized insurer. Section 1043, which authorizes the commissioner to enter into rehabilitation agreements, contains no express limitation on what may be included in them, and section 1037 provides that the enumeration of the powers of the commissioner shall not be construed as a limitation upon him or upon his right to do such other acts as he may deem necessary in connection with the handling of the affairs of an insolvent company.* [4] When salvaging the business of a seized insurer the greatest possible protection should be given to creditors and other interested parties, and in the present instance the commissioner evidently concluded that this objective could best be accomplished through the formation of a new company divorced as far as possible from the control of those who were in charge of the old company when it experienced financial difficulties.

[5] The new company is a separate and distinct entity, and when the business was transferred it ceased to be the business of the old company and became the business of the

* Section 1037 of the Insurance Code provides in part: "The enumeration, in this article, of the duties, powers and authority of the commissioner in proceedings under this article shall not be construed as a limitation upon the commissioner, nor shall it exclude in any manner his right to perform and to do such other acts not herein specifically enumerated, or otherwise provided for, which he may deem necessary or expedient for the accomplishmnt or in aid of the purpose of such proceedings."

BLEED THRU

new company. In *Garrison* v. *Pacific Mut. L. Ins. Co.*, 83 Cal.App.2d 1, 9-10 [187 P.2d 893], it was held that the identity of the new company "is utterly distinct from that of old company," and it "cannot be fairly said that it is a continuance of old company," and that the new company "is a separate entity that came into being after old company's insolvency was declared. . . ." [6] The fact that the new company may for some purposes have served as an agent or instrumentality of the commissioner does not destroy its identity as a separate company. [2b] Accordingly, as contemplated by the rehabilitation agreement, the applicable statutory provisions for mutualization of the new company are those found in section 11525 et seq., which govern voluntary mutualization of solvent nondelinquent insurers.

[7] Plaintiffs nevertheless contend that it was improper to follow the procedure set up in the code for mutualization of a solvent company because, they assert, the commissioner in doing so was forced to act in a dual capacity with conflicting interests. Section 11526, which prescribes the method to be followed in mutualizing a solvent insurer, provides that the plan shall be: ". . . . (b) Approved by the vote of the holders of at least a majority of the outstanding shares at a special meeting of shareholders called for that purpose, or by the written consent of such shareholders. (c) Submitted to the commissioner and approved by him in writing." Commissioner Carpenter as the sole holder of the stock of the new company consented in advance to the plan of mutualization, and Commissioner Downey approved it after holding a hearing to ascertain if the plan would be fair and equitable in its operation. Plaintiffs claim that the responsibilities of the commissioner under subdivision (c) are different from and may conflict with his duties under subdivision (b). Even if there might be such a conflict under some circumstances, it would not follow that it was improper to adopt the statutory procedure set forth for the mutualization of a solvent company. The legislative scheme for the mutualization of solvent nondelinquent insurers would in some instances be defeated if the commissioner were disqualified for the reasons urged by plain-

DARK PA

tiffs, and it must be assumed that the Legislature realized that the commissioner might be required to pass upon the fairness of a plan in a case where he, acting as conservator, had previously consented to mutualization on behalf of the stockholders. In numerous cases where the action of an administrative officer was necessary to prevent defeat of the statutory scheme, his participation has been upheld, although the grounds for disqualification were much more serious than those raised here. (For example, see *Thompson* v. *City of Long Beach*, 41 Cal.2d 235, 243-244 [259 P.2d 649]; *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 344, 365-366 [139 P.2d 908]; *Federal Const. Co.* v. *Curd*, 179 Cal. 489, 493-495 [177 P. 469, 2 A.L.R. 1202]; *Scannell* v. *Wolff*, 86 Cal.App. 2d 489, 492-493 [195 P.2d 536]; *Nider* v. *Homan*, 32 Cal.App.2d 11, 13 [89 P.2d 136].) The fact that Commissioner Carpenter gave advance consent on behalf of the stockholders to a plan of mutualization did not disqualify Commissioner Downey from passing upon the fairness of the mutualization plan which was promulgated.

An alternative reason for rejecting plaintiffs' claim that it was improper to follow the procedure set forth in section 11525 et seq. in the mutualization of the new company is that the validity of the rehabilitation agreement which provided for voluntary mutualization, is now res judicata. A copy of the agreement was attached to and made a part of the petition which sought approval of the agreement. The petition was filed pursuant to section 1043, which provides that rehabilitation agreements entered into by the commissioner are subject to the approval of the superior court. The validity of all the provisions of the agreement was put in issue by the petition and determined by the court. The order of December 4, 1936, approved the agreement "and each and all of the terms and conditions thereof, and the plan therein embodied," reciting that all interested parties had been given a reasonable opportunity to be heard on "the question of fairness, justice, equity, feasibility, and propriety" of the agreement and the plan. All parties were forever enjoined from making any complaint with respect to the agreement or any provisions thereof. This order was affirmed in *Carpenter* v. *Pacific Mut. L. Ins. Co.*,

E BLEED THRU

10 Cal.2d 307 [74 P.2d 761]. (See also *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 13 Cal.2d 306, 314-316 [89 P.2d 637]; *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 344, 351-352 [139 P.2d 908].)

[8] While different causes of action were involved in the present proceeding and the one leading to the order approving the rehabilitation agreement, the parties were the same, and it is settled that even though the causes of action be different, the prior determination of an issue is conclusive in a subsequent suit between the same parties as to that issue and every matter which might have been urged to sustain or defeat its determination. (*Shore* v. *Shore*, 43 Cal.2d 677, 682 [277 P.2d 400]; *Krier* v. *Krier*, 28 Cal.2d 841, 843 [172 P.2d 681]; *De Hart* v. *Allen*, 26 Cal.2d 829, 831 [161 P.2d 453]; *Estate of Keet*, 15 Cal.2d 328, 334 [100 P.2d 1045]; *Sutphin* v. *Speik*, 15 Cal.2d 195, 201 et seq. [99 P.2d 652, 101 P.2d 497]; *Caminetti* v. *Board of Trustees*, 1 Cal.2d 354, 356 [34 P.2d 1021]; *Price* v. *Sixth District Agri. Assn.*, 201 Cal. 502, 510 et seq. [258 P. 387]. Inconsistent language found in certain opinions of the District Court of Appeal must be disapproved. (*Green* v. *Green*, 66 Cal.App.2d 50, 59 [151 P.2d 679]; *Babcock* v. *Babcock*, 63 Cal.App.2d 94, 97 [146 P.2d 279]; *Bank of America* v. *McLaughlin*, 22 Cal.App.2d 411, 417 [71 P.2d 291, 72 P.2d 554].) [9a] The basic issue before the court when the agreement was submitted for approval was the propriety of each of its provisions, and the determination of that issue is conclusive as to every matter which might have been urged to sustain or defeat its determination.

It is contended that the order approving the rehabilitation agreement may be collaterally atacked upon the theory that the mutualization procedure provided for in the agreement followed the wrong statutory provisions and that therefore the order is void. For the purpose of passing upon this question we shall assume, contrary to what we have just decided, that the wrong statutes were used in the mutualization of the new company.

[10] It is the general rule that a final judgment or order is res judicata even though contrary to statute where the

DARK PA

court has jurisdiction in the fundamental sense, i. e., of the subject matter and the parties. [11] In the consideration of problems arising in this field it should be kept in mind that there is a difference between lack of jurisdiction in the fundamental sense, which is ordinarily essential for collateral attack, and the broader meaning of the term "lack of jurisdiction" when used in determining the availability of prohibition or certiorari to review an order or judgment. Some cases involving collateral attack have unfortunately failed to recognize this distinction. (For discussion of the distinction, see *Abelleira* v. *District Court of Appeal*, 17 Cal.2d 280, 287-291 [109 P.2d 942, 132 A.L.R. 715]; *Tide Water Assoc. Oil Co.* v. *Superior Court*, 43 Cal.2d 815, 821 [279 P.2d 35].)

[12] In some instances the requirements of a statute may relate to subject matter jurisdiction, and disregard of the statute may render a judgment void and subject to collateral attack. (See, for example, *Grannis* v. *Superior Court*, 146 Cal. 245, 254-255 [79 P. 891, 106 Am.St.Rep. 23]; *cf. Rogers* v. *Cady*, 104 Cal. 288, 291-292 [38 P. 81, 43 Am.St.Rep. 100] [constitutional provision].) [13] In the present case, however, it is clear that the court which approved the rehabilitation agreement had jurisdiction of the subject matter and the parties, and, unless the case comes within some exception, collateral attack cannot be based on the ground that the court authorized mutualization to proceed under the wrong statute.

[14] Closely analogous to the problem involved here are cases holding that probate decrees are res judicata, although they direct distribution pursuant to wills which are contrary to statute, since the court sitting in probate, like a court passing upon a rehabilitation agreement, is under a duty to determine the validity of the instrument before it. (*Estate of Loring*, 29 Cal.2d 423, 427 et seq. [175 P.2d 524]; *Crew* v. *Pratt*, 119 Cal. 139, 147 et seq. [51 P. 38]; *Estate of Gardiner*, 45 Cal.App.2d 559, 562 et seq. [114 P.2d 643]; *McGavin* v. *San Francisco P.O.A. Soc.*, 34 Cal.App. 168, 170 et seq. [166 P. 182].) [15] Similarly analogous are cases holding that an order settling a trustee's account is res judicata as to the propriety of the purchase of investment

E BLEED THRU

certificates which were issued contrary to statute. (*Wilson* v. *Security-First Nat. Bank*, 21 Cal.2d 705 [134 P.2d 800] *Estate of Crane*, 73 Cal.App.2d 93 [165 P.2d 940]; *cf. Fergodo* v. *Donohue*, 40 Cal.App. 670 [181 P. 819].) *Estate of Rowe*, 66 Cal. App.2d 594 [152 P.2d 765], which is contrary to the cases cited above, is disapproved.

[16] The principle of res judicata has also been applied as a basis for holding that judgments enforcing contracts are a bar to the defense of illegality in subsequent litigation. (*Andrews* v. *Reidy*, 7 Cal.2d 366 [60 P.2d 832]; *De Hart* v. *Allen*, 49 Cal.App.2d 639, 646 [122 P.2d 273], approved in *De Hart* v. *Allen*, 26 Cal.2d 829, 830-831 [161 P.2d 453]; *cf. Short* v. *Short*, 106 Cal.App. 210, 215 [288 P. 1111].) Another instance in which the doctrine was applied is *San Diego Trust & Sav. Bank* v. *Young*, 19 Cal.2d 98 [119 P.2d 133], where the prior judgment reduced the time for redemption contrary to statute. The San Diego case impliedly overruled *Anthony* v. *Janssen*, 183 Cal. 329 [191 P. 538], and *Tonningsen* v. *Odd Fellows' Cemetery Assn.*, 60 Cal.App. 568 [213 P. 710]. It has also been held that a judgment, which was contrary to the Constitution because it was based upon a statute later held invalid, was nevertheless res judicata in a subsequent suit, the court stating that objections to the statute should have been raised in the prior proceeding. (*Chicot County Drainage Dist.* v. *Baxter State Bank*, 308 U.S. 371, 376, 378 [60 S.Ct. 317, 319-320, 84 L.Ed. 329].) The Chicot case is quoted with approval in *Mueller* v. *Elba Oil Co.*, 21 Cal.2d 188, 205-206 [130 P.2d 961], and was cited in *Rescue Army* v. *Municipal Court*, 28 Cal.2d 460, 463-464 [171 P.2d 8].

There are some recognized exceptions to the general rule that collateral attack will not be allowed where there is fundamental jurisdiction even though the judgment is contrary to statute. [17] For example, a judgment may be collaterally attacked where unusual circumstances were present which prevented an earlier and more appropriate attack. (See 1 Witkin, California Procedure (1954), 411-412.) In *Burtnett* v. *King*, 33 Cal.2d 805 [205 P.2d 657, 12 A.L.R.2d 333], collateral attack was permitted against a default divorce decree which awarded all the community

DARK PAGE

property to the plaintiff in the absence of a prayer therefor in the complaint, contrary to the provision in section 580 of the Code of Civil Procedure that relief in a default case cannot exceed that demanded in the complaint. The defendant in the divorce action had no notice or warning that the property would be affected by a default judgment, and the opinion points out that the decision would sanction a trap if it held that his property rights had been disposed of since he would properly have assumed from the complaint that his rights to the property were not to be litigated at that time. (33 Cal.2d at p. 811.) The present case is readily distinguishable, since there was nothing to prevent the questions which are raised with regard to the validity of the rehabilitation agreement from being litigated in the proceedings which led to the order approving the agreement.

[18] Proceedings to prohibit or annul judgments of contempt for violation of injunctions and other equitable orders made contrary to statute may constitute another exception to the general rule. (*Harlan* v. *Superior Court,* 94 Cal.App.2d 902, 904-905 [211 P.2d 942]; *Hunter* v. *Superior Court,* 36 Cal.App.2d 100 [97 P.2d 492]; *cf. Fortenbury* v. *Superior Court,* 16 Cal.2d 405, 407-408 [106 P.2d 411] [violation of Constitution].) The decisions do not use the term, but the attack in such cases might be considered to be collateral, and the proceedings apparently fall in a special category because they are penal in nature.

[9b] From the foregoing discussion it follows that, even if we assume that the rehabilitation agreement and the order approving it authorized mutualization of the new company under the wrong statutes, the order is nevertheless res judicata.

The next problem is whether there was sufficient compliance with the statutory requirements for voluntary mutualization of solvent insurers. Section 11525 et seq. provide that the plan of mutualization shall be adopted by the directors and approved by the shareholders, the commissioner and the policyholders. Plaintiffs contend that the actions taken to meet these requirements were in certain respects defective and unauthorized.

BLEED THRU

The approval of the shareholders to the plan of mutualization was given in the rehabilitation agreement by Commissioner Carpenter as sole stockholder of the new company. As we have seen, the agreement provided for the formulation of a plan of mutualization by the price determination committee, and plaintiffs claim that the commissioner, acting for the shareholders of the new company, was without authority to give advance consent to such a plan. [19] In the absence of statutory provision to the contrary, the stockholders of a solvent company can contract to consent to a future plan of voluntary mutualization (*cf. Market St. Ry. Co.* v. *Hellman*, 109 Cal. 571, 585-587 [42 P. 225]), and no sound reason appears why such an agreement is improper merely because the shares are held by the commissioner as conservator of a seized insurer. The commissioner apparently concluded that a plan for mutualization which could not be destroyed by future action or nonaction of the shareholders was necessary as a means of inducing both former and prospective policyholders to deal with the new company and thus permit its continued existence. [20] The powers vested in the commissioner by sections 1037 and 1043 are sufficiently broad to authorize him, as sole stockholder, to give advance consent to the plan of mutualization. Moreover, the validity of all portions of the rehabilitation agreement, including the provision for advance consent, is res judicata.

The directors adopted the mutualization plan, but it is claimed that the action taken was ineffective because they assertedly did not obtain sufficient information to enable them to properly evaluate the desirability of the plan. [21] They had the benefit of the report of the price determination committee and the opinions of experts, including actuaries and officers of the company, and it seems obvious that, as a practical matter, directors must ordinarily act on the advice of corporate officers and other persons who have expert knowledge. (See Ballantine & Sterling, California Corporation Laws (1949), p. 110.)

After the directors adopted the plan as formulated by the price determination committee, Commissioner Downey held a hearing which lasted nearly three weeks. Oral and

DARK PAGE

documntary evidence was received, and all interested parties had an opportunity to participate. The commissioner approved the plan after finding that the rights and interests of the new company, its policyholders and shareholders were protected and that the plan would be fair and equitable in its operation. Plaintiffs contend that the findings are not supported by the evidence and that there was a lack of procedural due process at the hearing. In passing upon these contentions, we shall first give consideration to plaintiffs' claim that the trial court, in reviewing the action of the commissioner, should have held a trial de novo. [22] The approval of the mutualization plan by the commissioner did not involve any deprivation of property rights or vested rights; it was in essence a permit or license authorizing the new company to purchase its own stock. Under these circumstances the function of the superior court was to determine whether the action taken by the commissioner was arbitrary or constituted an abuse of discretion, and in upholding the action of the commissioner, it properly refused to conduct a trial de novo. (*Southern Calif. Jockey Club, Inc.* v. *California etc. Racing Board,* 36 Cal.2d 167, 174-175 [223 P.2d 1]; *McDonough* v. *Goodcell,* 13 Cal.2d 741, 746-749 [91 P.2d 1035, 123 A.L.R. 1205]; see *Thomas* v. *California Emp. Stab. Com.,* 39 Cal.2d 501, 504 [247 P.2d 561]; *Andrews* v. *State Board of Registration,* 123 Cal.App.2d 685, 694-695 [267 P.2d 352].)

[23] There is no merit in plaintiffs' claim that the record before the commissioner does not support his approval of the plan. The price determination committee consisted of men highly skilled in matters of insurance company valuation, and they were assisted in the formulation of the plan by Joseph Christman, associate actuary of the Metropolitan Life Insurance Company of New York, two Fellows of the Society of Actuaries, and numerous trained supervisory and clerical employees. Experts testified that the price fixed for the purchase of the stock was fair, that the provisions relating to the time and manner of payment were necessary for the safety and stability of the new company, that the proposed plan gave due regard and protec-

BLEED THRU

tion to the rights of all persons interested in the new company and would be fair in its operation.

[24] Plaintiffs' contention that there was a denial of procedural due process is based on their claim that the commissioner accepted the conclusions of the price determination committee without having before him all the facts on which those conclusions were based and that the committee itself relied on statistics furnished by its actuary without reviewing all the supporting data. Two members of the price determination committee testified in detail as to how the committee arrived at its determinations, and the actuary testified regarding his report which was introduced in evidence. Thus two of the four members of the committee who were responsible for its report, as well as the actuary who procured most of the data relied on by the committee, were available for cross-examination. These men, as we have seen, were experts in the insurance and investment fields, and the fact that the other members of the committee and the persons who assisted the actuary were not called as witnesses is immaterial, at least in the absence of a showing that plaintiffs sought to obtain their testimony. (*City of Pasadena* v. *City of Alhambra*, 33 Cal.2d 908, 919 [207 P.2d 17]. At the hearing an offer was made to furnish the documents and testimony necessary to explain every detail of the committee's work. No claim is made that any request for data was refused, and plaintiffs have no valid basis for complaint if they failed to make such a request.

The judgment is affirmed.

Shenk, J., Spence, J., and Wood (Fred B.), J., pro tem.,* concurred.

TRAYNOR, J.—I dissent.

Although the Legislature has provided detailed statutory provisions for the mutualization of the business of an insolvent insurer (Ins. Code, § 1045 et seq.), the majority opinion holds in effect that these provisions may be com-

* Assigned by Chairman of Judicial Council.

DARK PAGE

pletely nullified by the execution of a rehabilitation agreement under section 1043 of the Insurance Code, if such agreement provides for the voluntary mutualization of a new insurer created for the purpose of carrying on the business of the old. The commissioner has broad powers in executing rehabilitation agreements, and it may be both proper and desirable for him to make use of a new corporate entity to salvage the business of an insolvent insurer. It does not follow, however, that if the end product of a rehabilitation agreement is to be the mutualization of the business of an insolvent insurer, the statutory provisions with respect to such mutualization may be ignored. To hold that they may be not only renders the provisions with respect to involuntary mutualization superfluous but deprives the interested parties of their right to the protection of court scrutiny of the plan of mutualization. (See Ins. Code, § 1051.)

The importance to the shareholders of the old company of having the court independently pass upon the fairness of the plan of mutualization is demonstrated by the facts of this case. The trial court clearly indicated that had the decision been his, the plan would not have been approved; if the shareholders were entitled to his independent judgment, their rights have been prejudiced by his failure to exercise it. This case is not one involving only the mutualization of a solvent insurer, since if it were, the shareholders would have the power to protect their interests by withholding their consent to the plan of mutualization. (Ins. Code, § 11526, subd. (b).) In fact, the business of an insolvent insurer is being mutualized pursuant to a rehabilition agreement that has deprived the shareholders of the old company of the veto power they otherwise would have, and under the holding of the majority opinion they must look to the commissioner rather than to the court for the protection of their interests. (Ins. Code, §§ 11526, subd. (c), 11527.) Although the Legislature recognized that approval by the commissioner is sufficient when all of the interested parties are in a position to protect their own interests, it also provided that court approval is essential when they are not. (Ins. Code, § 1051.)

BLEED THRU

Despite the force of the foregoing considerations, if in fact the trial court in 1936 approved a rehabilitation agreement that not only provided for mutualization contrary to the statutory provisions but also restricted the power of that court to control the ultimate disposition of the assets in the hands of the commissioner as conservator or liquidator, I would reluctantly concur in the judgment on the ground that the validity of the agreement and order is res judicata. In my opinion, however, the court in 1936 did not exhaust its power to control the disposition of assets in the hands of the commissioner as conservator or liquidator (see Ins. Code, § 1037, subd. (d)) and that therefore the commissioner cannot carry out the terms of the mutualization agreement until as liquidator he has secured the permission of the court in the insolvency proceedings. Accordingly, until he secures that approval he cannot approve the plan presented by the price determination committee as "fair and equitable in its operation" (Ins. Code, § 11527), for it cannot be known whether it will become operative at all until it is approved by the court in the insolvency proceedings.

Subdivision (d) of section 1037 provides "that no transaction involving real or personal property shall be made where the market value of the property involved exceeds the sum of one thousand dollars without first obtaining permission of . . . [the court in the insolvency proceedings], and then only in accordance with such terms as said court may prescribe." The stock of the new company subject to the plan of mutualization is personal property worth more than $1,000, and that plan is clearly a transaction involving such property. This section has not been complied with unless the court in approving the rehabilitation agreement granted permission to the commissioner to dispose of the stock under the terms of any mutualization agreement that might be proposed by the price determination committee 10 years or more in the future.

The order approving the rehabilitation agreement is ambiguous. Paragraph 15 provides:

"That the Insurance Commissioner of the State of California as Conservator of respondent corporation, or, if he

DARK PAGE

should hereafter be appointed Liquidator of said corporation, as such Liquidator, be and is hereby authorized, without further order of this court, fully and faithfully to perform, carry out, and discharge each and all of the obligations, terms, conditions, and covenants on his part required to be performed under the terms of said Rehabilitation and Reinsurance Agreement; and, either with or without further order of this court, to make, do, execute, and deliver any and all such further or other acts, deeds, and things by him deemed reasonably necessary or desirable to effectuate the intents and purposes of said Rehabilitation and Reinsurance Agreement, and to assure and to confirm to Pacific Mutual Life Insurance Company, or its successors, all and singular the properties hereinbefore directed to be conveyed and released to said corporation, and to enable said corporation from and after the date hereof to conduct and continue to conduct a life and disability insurance business, as contemplated by said agreement."

Paragraph 16 provides:

"That this court, without relinquishing by these specific provisions any jurisdiction by it retained as a matter of law, do, and it does hereby, specifically retain and reserve jurisdiction of the within proceedings (for the purpose of authorizing or approving any act of the Insurance Commissioner of the State of California done, or to be done pursuant to or in accordance with this order, and) for the purpose of making or entering, upon application of the Insurance Commissioner of the State of California or of Pacific Mutual Life Insurance Company, any order, decree, judgment, or ruling required, permitted, or requested to be done, made, or entered in connection with or pursuant to the terms of said agreement, or for the effectuation of the purposes thereof."

Since the contemplated plan of mutualization was not to be formulated for at least 10 years, the court could obviously not approve that plan at the time it entered its order approving the rehabilitation agreement. Moreover, it did not expressly approve in advance the carrying out of any mutualization plan that might be presented by the price

LEED THRU

determination committee. Although standing alone the language permitting the commissioner to carry out the rehabilitation agreement "without further order of this court" might be interpreted as exhausting the court's jurisdiction over mutualization, it may not reasonably be so interpreted in the light of the express reservation of jurisdiction "for the purpose of making . . . any order . . . required . . . in connection with or pursuant to the terms of said agreement." It is significant that in *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal.2d 307, 322 [74 P.2d 761], this court was careful to note: "The plan also provides that the commissioner, either as conservator or liquidator, shall continue to hold all the stock of the new company as a protection to all old company policyholders. Ultimate mutualization, in the event the policyholders so elect is also provided for. The trial court reserves jurisdiction over the entire proceeding." Paragraphs 15 and 16 may be reconciled by interpreting them as authorizing the commissioner without further order of the court to carry out the rehabilitation agreement to the extent that its provisions represented a completed plan for rehabilitation and reinsurance, and at the same time reserving to the court jurisdiction to approve or disapprove plans to be developed in the future for mutualization or other disposal of the stock in the hands of the commissioner. Such an interpretation of the order subserves the primary purpose of section 1037, subdivision (d), and the statutes governing involuntary mutualization by securing to all interested parties their right to court scrutiny of all steps in the proceedings that substantially affect their rights, and since the order is reasonably susceptible of that interpretation it should be adopted. Although the validity of the rehabilitation agreement and the order approving it are res judicata, the interpretation of the order is not res judicata, and it should not be interpreted to sanction further departures from the statutory provisions than res judicata compels. (See *Watson* v. *Lawson*, 166 Cal. 235, 242 [135 P. 961]; *Treece* v. *Treece*, 125 Cal.App. 726, 728 [14 P.2d 95].)

The judgment should be reversed.

Schauer, J., concurred.

DARK PAGE

CARTER, J.—I dissent.

The majority opinion is a masterpiece of legal legerdemain. It approves a transaction whereby the policyholders of old company are deprived of between $18,000,000 and $24,000,000 to which they are entitled under any concept of law and justice. It also deprives the stockholders of old company of whatever value their stock in old company may be worth in view of the fact that the assets of old company which were transferred to new company at the time of its creation were valued in excess of over $200,000,000. The majority concedes that new company was created in an insolvency proceeding and has always been used in said proceeding as an agency of the insurance commissioner for the purpose of rehabilitating an insolvent insurance company, and that such proceeding is still pending because rehabilitation has not been completed. It nevertheless holds that "the new company is solvent and nondeliquent," even though it owes and is obligated to pay the policyholders of old company between $18,000,000 and $24,000,000 which it admittedly is not financially able to pay. In approving this transaction the majority disregards express statutory provisions of this state and deprives the stockholders and policyholders of old company of their right to a judicial review of the administrative proceeding whereby they were deprived of their property, thus denying them due process of law to which they are entitled under both state and federal constitutional provisions.

The Undeniable Facts

On July 22, 1936, some 3,000 stockholders and 300,000 policyholders of The Pacific Mutual Life Insurance Company of California, hereinafter known as old company, were stunned by the news that the insurance commissioner had taken charge of the company, alleging it to be insolvent. This development was all the more shocking because of its suddenness and also because only a short time before, the regular, verified, annual statement of the company showed it to be in sound financial condition, as had similar previous statements from year to year consistently

BLEED THRU

shown throughout its lifetime of over 68 years. The business and assets of old company were then taken over by the insurance commissioner of this state pursuant to the provisions of sections 1011 and 1013 of the Insurance Code. Thereafter, The Pacific Mutual Life Insurance Company was organized as part of a plan of rehabilitation of old company by the commissioner who purchased its entire capital stock with assets of old company. Pursuant to section 1043 of the Insurance Code, a "Rehabilitation and Reinsurance" agreement was entered into between the new company and the then insurance commissioner, as conservator of old company. The rehabilitation plan provided for the organization of a new corporation with a capital of $1,000,000 which consisted of 10,000 shares at a par value of $100 each. The commissioner was to purchase all the outstanding stock of the new company with $3,000,000 in cash belonging to the old company (which gave new company an initial surplus of $2,000,000). The commissioner was then to transfer all the other assets of old company (with the exception of the stock of new company which, of course, was owned by old company) to new company, and new company was to assume all policies and obligations of the old company to the extent provided for in the plan. The plan provided that new company would assume all the obligations of the old company under existing policies with the exception of the non-can policies, which obligations were assumed on a reduced benefit schedule at the old premium rates. It was agreed that further benefits would be restored out of certain designated income of new company. *All of new company's stock was purchased with $3,000,000 out of old company's funds.* In addition, all the other assets of old company (over $200,000,000 assets in addition to going agency organization and concern, good will, etc., "worth several millions of dollars" [*Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal.2d 307, 325 [74 P.d 761]) were transferred to new company. Therefore, new company owes its creation and existence to old company. The confiscatory nature of this entire proceeding, including the present majority holding, is at once apparent when we see that old company's stockholders will ultimately only receive $3,000,000 for their stock which, when old company was

DARK PAGE

taken over, was supported by that amount in cash *plus* over $200,000,000 in various assets plus the value of good will, going business organization, etc., worth several millions of dollars! The agreement thus provided for a transfer to new company of the assets of old company (with certain exceptions not relevant here) and the assumption by new company of the obligations of old company, excluding certain noncancellable policies. With regard to these policies, known as the "non-can" policies, new company assumed a limited obligation and agreed to set up a special fund for the restoration of benefits thereunder. This obligation is still unpaid and outstanding. The capital stock of new company was to be held by the commissioner, as conservator, or liquidator, for the benefit of the creditors, policyholders, and stockholders of old company. On December 4, 1936, the agreement was approved by the trial court. In *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal.2d 307, 332, 334 [74 P.2d 761 (affirmed *Neblett* v. *Carpenter*, 305 U.S. 297 [59 S.Ct. 170, 83 L.Ed. 182]), it was held that the organization of new company, as part of a plan to rehabilitate the business of old company was proper. It is pointed out (p. 322) that "Ultimate mutualization, in the event the policyholders so elect is also provided for."

On February 2, 1937, an order was made providing for the liquidation of the old company and appointing the insurance commissioner as liquidator. This order was upheld on appeal (*Carpenter* v. *Pacific Mut. L. Ins. Co.*, 13 Cal.2d 306 [89 P.2d 637]), although old company has never been dissolved. On April 4, 1938, the commissioner, as liquidator, transferred title to the capital stock of new company to voting trustees. This transfer was upheld on appeal (*Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 344 [139 P.2d 908]). (Other aspects of this case have been decided by this court in *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 77 [136 P.2d 779]; *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 386 [139 P.2d 930]; *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 23 Cal.2d 94 [142 P.2d 741]; *Neblett* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 393 [139 P.2d 934]; *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 14 Cal.2d 704 [96 P.2d 796]; and by the appellate courts in *Sanborn* v. *Pacific Mut. L. Ins. Co.*,

BLEED THRU

42 Cal.App.2d 99 [108 P.2d 458]; *Garrison* v. *Pacific Mut. L. Ins. Co.*, 83 Cal.App.2d 1 [187 P.2d 893].)

New company now seeks to acquire its stock (see later discussion) through the device of mutualization under section 20(a) of the rehabilitation agreement. The mutualization plan provides that the price to be paid for new company's stock is $3,000,000, with simplet interest. If non-can benefits are fully restored prior to January 1, 1973, the purchase price is to be increased by an additional sum of $250,000 for each full year by which the date of completion of restoration precedes December, 1973. The purchase price is not absolutely payable, but is to be paid only "when and if" all the following conditions are met: (1) Non-can restoration is completed; (2) the funds in a special surplus fund (to be created pursuant to the plan) plus the capital and surplus of new company, equal or exceed the purchase price of the stock; (3) the *financial condition* of the *new company* is such that, after paying for and cancelling the stock, it would still have admitted assets in excess of all its liabilities amounting to the sum of 4 percent of all admitted assets plus 25 per cent of the premiums collected during the preceding calendar year on all group insurance written on a one-year term basis and on all accident and health insurance.

This resume shows that the new company was brought into existence as a creature of the state to rehabilitate old company and to carry on its business for that purpose. It also shows the grievous injustice being perpetuated by the majority in approving the plan of mutualization used here —that of *voluntary* mutualization of an *insolvent* corporation. This type of voluntary mutualization is as voluntary as a confession given under force, duress, and threats of injury. Non-can benefits have not been fully restored; even under the mutualization plan it is contemplated they will not be fully restored (if partial benefit payments can be considered "full" restoration) until 1973. Until such time as they are restored, new company cannot be considered as a solvent concern since it still owes a debt to the policyholders and stockholders of old company, which it admittedly *cannot now pay*. The amount of this debt is

conceded to be between $18,000,000 and $24,000,000. How can it then be said, with any degree of honesty whatsoever, that new company is solvent and may avail itself of the statutory provisions relating to mutualization? I defy anyone to give an affirmative answer to this question.

Present Proceeding

Purporting to act under paragraph 20(a) of the rehabilitation and reinsurance agreement, a plan of mutualization was formulated by the committee and, on September 22, 1950, the insurance commissioner found that the plan protected the rights and interests of new company, its policyholders and shareholders, and that he was satisfied that the plan would be fair and equitable in its operation.

Paragraph 20(a) of the rehabilitation and reinsurance agreement provides:

"Mutualization and Disposition of Stock of New Company

"(2) Neither the Conservator, nor, if one be appointed, the Liquidator, of the Old Company, shall dispose of any of the stock of the New Company except as follows:

"(a) At any time between July 1, 1946 and January 1, 1948, and thereafter so long as the Conservator or a Liquidator of the Old Company may continue to hold any or all of said stock, ten percent (10%) of the holders of participating policies of life insurance entitled to vote at a policy holders' election on a proposal for *voluntary* mutualization of the New Company, whether those re-insured hereunder or those issued by the New Company (each policy holder for this purpose being regarded as one person regardless of the number of policies owned or amount of insurance held) may request the New Company to create an Appointing Committee as hereinafter provided to exercise the duties and functions hereinafter specified in respect of a proposed *voluntary* mutualization of the New Company, in accordance with the laws of the State of California in effect at the time of said request, or, if said laws then so permit, of any one or more departments thereof.

Such request shall specify the department or departments of the New Company desired to be mutualized.

"Upon the receipt of such request the New Company shall create an Appointing Committee consisting of the then President of the Association of Life Insurance Presidents, the President of Leland Stanford Jr. University, and the Provost of the University of California at Los Angeles, or persons occupying similar positions if their or any of their titles shall have been changed. In the event any one or more of such persons shall refuse or be unable to act, the remaining member or members shall fill the vacancy or vacancies thereby created by their appointment in writing of another person or persons of similar position and standing. If all of said persons refuse or are unable to act, the Court or any Judge thereof shall, on the application of the Commissioner, designate an Appointing Committee consisting of three (3) persons of similar position and standing. Said Appointing Committee, acting through not less than a majority of its members, shall designate a Price Determination Committee of not less than three and not more than five (5) persons skilled in matters of insurance company valuation, which committee, acting through not less than a majority thereof, shall determine whether in their opinion the proposed *voluntary* mutualization of the New Company, or of the department or departments thereof specified in said request can then be practicably accomplished *having due regard to the interests of all persons interested in the New Company.** If it can be determined that such mutualization is not then practicable no further steps shall be taken in connection with a possible mutualization of the New Company under the provisions of this subparagraph until at least six months after the date of such determination. If in the opinion of a majority of the members of the committee such mutualization is then practicable, the committee shall determine the proper price to be paid upon such mutualization and appropriate terms of payments

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* The statutory scheme relating to insolvent companies is concerned with the protection of those interested in the *insolvent* company.

DARK PAG

thereof; said determination shall not be made, however, prior to January 1, 1947.

"If, at the date of the appointment of such committee the New Company shall have in force Participating Life Insurance written subsequent to the effective date of this agreement in an amount in excess of its Non-Participating Life Insurance written during the same period, one-half (½) of such excess shall, for the purpose of fixing the proper price to be paid (but for no other purpose) be deemed to be, and shall be valued as, Non-Participating Life Insurance. If at the time of such appointment, there shall have been transferred from the Participating Department in accordance with the provisions of sub-paragraph (d) of paragraph 6 hereof, less than ten percent (10%) of the then accrued earnings described therein, or if there shall have been transferred to the Participating Department any working capital pursuant to the provisions of subparagraph (c) of said paragraph 6, any unpaid balance thereof shall, for the purpose of fixing the proper price to be paid (but for no other purpose) be deemed to be a debt then due and matured. Said Committee shall in its report to the New Company include a plan of mutualization of the New Company, or of the department or departments thereof specified in said request of the policy holders. Such plan shall specify, in addition to any other relevant matters, the price to be paid, the terms of payment, and the persons by whom and the manner in which the right to vote the stock of the New Company is to be exercised pending complete payment of the purchase price. In this connection the said Committee, if it deem it advisable, may provide in the plan for the creation of a voting trust, designate the initial trustees, and make provision for the appointment of their successors. Unless the benefits under Non-Can policies have theretofore been fully restored and claims against the Liquidator fully paid, such plan shall further provide that such mutualization shall not affect the provisions of paragraph 17 or of paragraph 14 hereof or the right of holders of Non-Can Policies to the restoration of benefits from the sources and in the manner therein provided.

BLEED THRU

"The New Company agrees that within sixty (60) days after the making of such report (unless said report shall be to the effect that mutualization is not then practicable) it will mail copies thereof to all of its policy holders entitled to vote upon such plan or plans of mutualization if submitted according to law. If within one hundred twenty (120) days after the mailing of such notice, ten per cent (10%) of the policy holders entitled to vote upon any such plan or plans (each policy holder being for this purpose regarded as one person regardless of the number of policies owned or amount of insurance held) shall request in writing the submission thereof, the New Company will promptly submit the same in accordance with the laws of the State of California then in effect. The Conservator for himself and for any successors in the ownership of said stock claiming under him in any manner other than through a sale of said stock pursuant to the provisions of subparagraph (d) hereof agrees to consent and hereby consents as the holder and owner of the stock of the New Company to such plan of mutualization. In the event said mutualization plan is adopted, the Conservator, or a liquidator as aforesaid, shall dispose of such stock in accordance with such plan. The expenses of the foregoing proceedings including costs, fees and expenses of the Price Determination Committee, shall be borne by the New Company, and unless the proposed plan of mutualization is consummated, shall be charged to the Participating Department thereof.

"In the event the Price Determination Committee has been appointed as herein provided prior to January 1, 1948, said Committee shall have the power to extend the time within which mutualization may be effected hereunder for such period or periods of time as it may deem necessary for the orderly completion of mutualization proceedings as herein ordered." (Emphasis added.)

Mutualization

The Insurance Code provides for mutualization of insurance companies in two different ways. Division 1, part 2, chapter 1, article 14, sections 1010-1062, entitled "Proceedings in Cases of Insolvency and Delinquency" provides

DARK PAG

in section 1043 for "Mutualization, reinsurance and rehabilitation." Division 2, part 2, chapter 13, article 1, sections 11525-11533, entitled "Voluntary Mutualization of Incorporated Life and Life and Disability Insurers Having a Capital Stock and Issuing Nonassessable Policies on a Reserve Basis" provides in sections 11525 and 11526 the "Authorization to mutualize" and the "Method of mutualization."

There is no dispute concerning the method actually used in this proceeding. The rehabilitation plan provided for "voluntary" mutualization and the matter proceeded under sections 11525 and 11526. There is complete disagreement as to which method should have been used. Appellants correctly contend that the procedure outlined for "involuntary" mutualization of an "insolvent" insurer is the only proper method.

As stated in *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal.2d 307, 328 [74 P.2d 761], ". . . the proceedings here under review were taken under sections 1010 to 1061 of the Insurance Code, adopted in 1935." (The other cases heretofore cited have reiterated this statement.) The original seizure of old company was accomplished under section 1011, subdivision (d). Section 1045 provides *"Mutualization of life insurer issuing nonassessable policies on a reverse basis: Formation of plan.* If at any time *after the issuance of an order under section 1011* affecting a life insurer issuing nonassessable policies on a reserve basis and organized with a capital stock evidenced by shares thereof *it shall appear to the commissioner that the purposes of section 1011 can be best attained by the mutualization of such life insurer, the commissioner may formulate a plan for the mutualization of such insurer."* (Emphasis added.)

All proceedings heretofore had in this litigation have been as provided for in article 14 relating to insolvent and delinquent insurers. The rehabilitation agreement provides for mutualization under the statutory scheme set up for solvent insurers. The majority opinion states "The new company is solvent and nondelinquent, and there is no

BLEED THRU

sound reason why it should be mutualized under the statutes relating to insolvent insurers. . . . Section 1043 [which relates to insolvents], which authorizes the commissioner to enter into rehabilitation agreements, contains no express limitation on what may be included in them, and section 1037 [which also relates to insolvents] provides that the enumeration of the powers of the commissioner shall not be construed as a limitation upon him or upon his right to do such other acts as he may deem necessary in connection with the handling of the affairs of an *insolvent company.*" (Emphasis added.) Thus the majority opinion admits the procedure relating to insolvents was the one used and impliedly admits that it is the correct procedure. However, in using the code sections relating to insolvents, the author then argues that these sections place no limitation upon the commissioner. Section 1037 provides that the powers and authority of the commissioner in proceedings "*under this article*" (which relates to insolvents) shall not be construed as a limitation on his right to act or to do that "which he may deem necessary or expedient for the accomplishment or in aid of the purpose of *such proceedings.*" Then, citing section 1043 (relating again to insolvents), we are told that the new company was properly organized by the commissioner who "evidently concluded" that the protection of creditors and "other interested parties" could best be accomplished through the formation of a new company "divorced as far as possible from the control of those who were in charge of the old company when it experienced financial difficulties." Then we are told that the new company is a separate and distinct entity. We are told this without any discussion of the character of new company, and with only the unreasoned and unsupported dictum in *Garrison* v. *Pacific Mut. L. Ins. Co.*, 83 Cal.App.2d 1, 9-10 [187 P.2d 893], as authority therefor.

Section 11525 (the procedure followed here) provides for "*Authorization to mutualize.* A *solvent* domestic incorporated insurer having a paid-in capital represented by outstanding shares of capital stock and issuing, on a reserve basis, nonassessable policies of life insurance or of both life

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and disability insurance, *may convert itself into an incorporated mutual life insurer,* or life and disability insurer, issuing nonassessable policies on a reserve basis. To that end *it may provide and carry out a plan for the acquisition of the outstanding shares of its capital stock for the benefit of its policyholders,* or any class or classes of its policyholders, by complying with the requirements of this chapter." (Emphasis added.)

The question is thus directly posed as to whether new company falls within the classification of a "solvent" domestic incorporated insurer which "may convert itself into an incorporated mutual life insurer" which "may provide and carry out a plan for the acquisition of the outstanding shares of its capital stock for the benefit of its policyholders."

Character of New Company

New company was organized by the insurance commissioner "with a name similar to that of the old company as a corporate agent to assist him in carrying on the business of the old company" (*Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal.2d 307, 324, 325 [74 P.2d 761]). It was also said there (p. 327) that "The proceeding was had under sections 1010 to 1061 of the Insurance Code which specially deal with the rehabilitation and liquidation of insurance companies. Those sections set up a comprehensive statutory scheme to accomplish those results. The proceeding is not one in which another party is prosecuting another party at all. It is simply a proceeding in which the state is invoking its power over a corporate entity permitted by the state to engage in a business vitally affected with the public interest upon condition of continuing compliance with the requirements provided by the state. It is not a controversy between private parties but a proceeding by the state in the interest of the public." See also *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 77, 82 [136 P.2d 779], where it was held that *"The new company was the corporate agency of the Insurance Commissioner as conservator for the purpose of continuing and preserving the business of the old company."* (Emphasis added.)

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The commissioner held, either as conservator or later as liquidator, the entire capital stock of new company until 1938 when it was transferred to voting trustees (*Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 344, 356 [139 P.2d 908]). It was there said that "The affairs of the new company are placed in charge of a board of directors to whom the agreement expressly confides a large measure of discretion. *Supervisory powers, however, are reserved to the commissioner,* independent of and in addition to his statutory powers over delinquent insurance companies. For example, no investment or reinvestment of the assets of the old company may be made without written approval of the commissioner. Payments to the restoration fund for non-can policies are subject to the approval of the commissioner who, in addition, may require further payments thereto. The determination by the board of directors of the apportionment of expenses and the exchange of assets among the several departments of the new company is subject to adjustment by the commissioner. Reserves against policies of the old company subject to assumption or reinsurance under the agreement were to be established by the new company *with the approval of and in accordance with the requirements of the commissioner.* While as holder of the stock the commissioner possessed the voting rights incident thereto, the agreement contains no express provision with respect to the exercise of the voting power. . . .

"The trustees are given legal title to the stock of the new company with the power to exercise all the rights of ownership. *The commissioner, however, retains the entire beneficial interest for the benefit of creditors of the old company and others interested. The voting trust undertakes to transfer to the trustees only administrative duties relating to the stock, principally the right to vote the same. . . .*" (Emphasis added.)

New company does not possess the characteristics of a solvent company as that term is generally understood. First, it was organized as the *agent* of the *commissioner* to *rehabilitate* the *business* of the *old company.* It may be, as was said in the Garrison case, that it is a distinct entity

DARK PAG

without detracting in the least from the fact that it is still an agent for the purpose of rehabilitating the old company. An agent, or servant, is usually a distinct entity, but the duties and activities of such agent or servant, are carried out to serve the purposes of the principal. In other words, the agent acts for the principal, not for himself, or itself. Does the insurance commissioner ordinarily, and customarily, hold all the stock of a solvent insurance company? Does the insurance commissioner ordinarily, and customarily, have reserved to himself supervisory powers, "independent of and in addition to his statutory powers" where a solvent company is concerned? Does an insurance commissioner ordinarily, and customarily, give his written approval of the investment or reinvestment of funds of a solvent insurance company? Does the insurance commissioner ordinarily, and customarily, tell the board of directors of a solvent company when and how they must apportion expenses and exchange assets among its several departments? In the case of new company, the commissioner does all of those things. (See Chief Justice Gibson's opinion in *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 344, 356 [139 P.2d 908].)

New company would have no existence had it not been for the technical insolvency of old company. No new money constituted the assets of new company which was organized with the assets of old company. If new company were a solvent independent and distinct corporation, the insurance commissioner would not be holding its stock for the policyholders of old company. The stockholders of new company would be holding their own stock supported by assets in the hands of the officers and directors of the company. Section 11525 provides that "A solvent domestic incorporated insurer [is one] having a paid-in capital represented by outstanding shares of capital stock and issuing, on a reserve basis, nonassessable policies of life insurance or of both life and disability insurance. . . ." Surely in the normal case, "outstanding shares of capital stock" refers to stock held by stockholders, *not* by the commissioner!

Mr. Justice Traynor has pointed out how the use of the solvent mutualization procedure has deprived the members

BLEED THRU

of old company of their right to the protection of court scrutiny of the plan of mutualization. He shows how the procedure used here cannot apply to the facts of the case because in the ordinary case of a voluntary mutualization, the shareholders would have the power to protect their interests by withholding their consent to the plan of mutualization. The sections of the code which relate to mutualization of insolvent companies were clearly intended by the Legislature to protect the interests of the interested parties by providing for court approval.

In the present case by the use of the procedure provided for in the case of a solvent company, the commissioner approves a plan to be formulated in the future. When that plan is formulated, as holder of all the stock, he votes for the plan. Then, as commissioner, he approves the plan as fair and equitable. We are told by the majority opinion that "it must be assumed that the Legislature realized that the commissioner might be required to pass upon the fairness of a plan in a case where he, acting as conservator, had previously consented to mutualization on behalf of the stockholders." Nothing of the kind must be assumed. It is obvious from even a casual reading of the code provisions relating to insolvent companies (1043 et seq.) and those relating to solvent companies (11525 et seq.) that the Legislature had not the faintest thought that the two would be so commingled as they are in this case, or that the commissioner would be placed in a position where he was forced to approve a plan to be formulated some 10 years in the future, then, when the plan was formulated forced to vote an approval of it as a sole stockholder, and still later, to give his approval of something he had theretofore twice before approved.

Ever since the inception* of the receivership proceedings and the organization of new company all the parties and proceedings concerned in the rehabilitation matter have been subject to the continuing jurisdiction and supervision of the court. It has been pointed out in various

* (With the exception of the present proceeding to be hereinafter discussed.)

DARK PAG

phases of this litigation that new company was organized by the commissioner as his *corporate agent* to rehabilitate the business of old company. Without the original proceeding under section 1011 (d) of the Insurance Code, new company would not have come into being.

It is necessary, next, to note the difference in methods provided for in the two divisions of the Insurance Code for mutualization of insolvent and solvent companies.

Section 1046 provides that "Said mutualization plan [called involuntary mutualization for insolvent companies and follows the section (1045) which provides: "If *at any time after the issuance of an order under section 1011*" the "*commissioner*" shall formulate a plan of mutualization] *shall* include provisions for:

"(a) [Acquisition of capital stock.] The acquisition by such insurer of all outstanding shares of its capital stock at a price and upon terms and conditions to be fixed as hereinafter provided.

"(b) [Retirement of capital stock.] The retirement of said shares of stock when acquired by such insurer.

"(c) [Amendment of charter.] The amendment of the charter of such insurer so as to enable it to transact its business as a mutual insurer issuing nonassessable policies on a reserve basis.

"(d) [Payment of claims.] The manner in which and the time within which, after mutualization is effected, matured and maturing claims against such insurer shall be paid to the lawful holders thereof.

"(e) [Submission of plan to policyholders.] The submission of said mutualization plan to the policyholders of such insurer under such procedure as shall be set forth in the plan or prescribed by said court, for their approval or rejection.

"(f) [Notice to shareholders.] Notice to the shareholders of such insurer, in such manner and at such time after the approval of said mutualization plan by said policyholders, as the court may direct."

BLEED THRU

Section 1048 provides that after the formulation of the mutualization plan, the commissioner shall submit it to the court for its order directing the submission thereof to the policyholders named in subdivision (e), of section 1046.

Section 11526 (relating to *solvent* insurers) provides that "Such plan shall include appropriate proceedings for amending the insurer's articles of incorporation to give effect to the acquisition, by said insurer, for the benefit of its policyholders or any class or classes thereof, of the outstanding shares of its capital stock and the conversion of the insurer from a stock corporation into a nonstock corporation for the benefit of its members. The members of such nonstock corporation shall be the policyholders from time to time of the class or classes for whose benefit the stock of the insurer was acquired, and no other persons. Such plan shall be:

"(a) Adopted by a vote of a majority of the directors. [As distinguished from the formation thereof by the commissioner as provided in section 1045.]

"(b) Approved by the vote of the holders of at least a majority of the outstanding shares at a special meeting of *shareholders* called for that purpose, or by the written consent of such shareholders. [As distinguished from section 1048 requiring the commissioner to obtain court approval and an order of the court directing the submission of the plan to the policyholders.]

"(c) Submitted to the commissioner and approvad by him in writing. [Under the circumstances here prevailing with regard to the commissioner's position as conservator, liquidator and general supervisor of new company, this amounts to an idle act.]

"(d) Approved by a majority vote of all the *policyholders* of the class or classes for whose benefit the stock is to be acquired voting at an election by the policyholders called for that purpose, subject to the provisions of section 11528. . . .

DARK PAG

"(e) Filed in the office of the Insurance Commissioner after having been approved as provided in subdivisions (b), (c) and (d) of this section."

Under the provisions of the rehabilitation agreement, a price determination committee consisting of four members was set up. The price determination committee reported to new company, in April, 1950, that mutualization was practicable and valued the stock of new company at $3,000,000. The mutualization plan provided in part for the payment of the purchase price with simple interest at the rate of long term government bonds (2½%). Under the terms of the rehabilitation agreement, "The Conservator for himself and for any successors in the ownership of said stock claiming under him in any manner other than through a sale of said stock pursuant to the provisions of sub-paragraph (d) hereof agrees to consent and hereby consents as the holder and owner of the stock of the New Company to such plan of mutualization. In the event said mutualization plan is adopted, the Conservator, or a Liquidator as aforesaid, shall dispose of such stock in accordance with such plan."

Under the voluntary mutualization procedure heretofore set forth (section 11526) the mutualization plan is submitted to the commissioner after adoption by a vote of a majority of the directors and after a vote by a majority of the outstanding shares at a special meeting of shareholders called for that purpose. Section 11527 provides that "The Commissioner shall examine the plan submitted to him under the provisions of subdivision (c) section 11526. *He shall not approve such plan unless in his opinion the rights and interests of the insurer, its policyholders and shareholders are protected nor unless he is satisfied that the plan will be fair and equitable in its operation.*" (Emphasis added.) Fair and equitable to *which* company?

Under the provision of the rehabilitation agreement heretofore set forth, the then commissioner agreed for himself, and his successors, to agree to any plan promulgated by the price determination committee. It should be borne in mind that the stock of new company is now held

BLEED THRU

by voting trustees who had no discretion, but were (as stated in the insurance commissioner's answering brief, p. 73) "not only *authorized*, but *bound* to give their consent; and [that] they had no discretion to exercise." (Emphasis that of the commissioner.) There is evidence in the record which shows that the trustees voted for the plan of mutualization because they were told to so vote; that they did not examine into the merits of the plan. The next step provided for in section 11526 (Ins. Code) is that the plan shall be submitted to the commissioner for his written approval. The insurance commissioner states (Answering brief, p. 83), "As we have already shown, the Liquidator [commissioner] has bound himself to consent to a Plan of Mutualization proposed in accordance with the Rehabilitation Agreement." The code, however, (§ 11527) provides that the commissioner shall examine the plan submitted to him under the provisions of subdivision (c) of section 11526 and that "*He shall not approve such plan unless in his opinion the rights and interests of the insurer, its policyholders and shareholders are protected nor unless he is satisfied that the plan will be fair and equitable in its operation.*" (Emphasis added.) The net result, under the circumstances prevailing in this case, is that the commissioner, as beneficial owner of all the stock of the new company, instructs the voting trustees to vote for any plan proposed by the price determination committee and then, when such plan is submitted to him for his approval, places his rubber stamp of approval thereon because he (or his predecessor) has, 10 years prior to the promulgation of the plan, agreed to approve it *no matter what it is*—agreed, not only for himself, but for any successor in office, to approve the plan as proposed. It is shown, therefore, without a shadow of a doubt, that the earlier agreement to approve any plan proposed by the price determination committee has the effect of nullifying section 11527 of the Insurance Code, as well as the sections relating to mutualization of insolvent insurers.

Had the procedure outlined in sections 1045, 1046 and 1048 been followed, the result would be very different. Under section 1045 the *commissioner* would formulate the

DARK PAGE

mutualization plan for the purpose of carrying out the rehabilitation of the insurer whose business was seized under the provisions of section 1011 The commissioner's plan would then be submitted to the court for its order directing the submission of the mutualization plan to the shareholders and policyholders of the seized insurer for their vote of approval, or disapproval as the case might be (§ 1046, subds. (e) and (f)). Old company, not having been dissolved, still exists; new company was organized as the corporate agent of the commissioner to rehabilitate the business of old company with the assets of old company. New company cannot, as it appears, be considered as a completely independent and solvent organization under the facts here prevailing. As I have pointed out, the commissioner holds the entire beneficial interest in all the capital stock of new company for the benefit of stockholders, policyholders and creditors of old company; the legal title to the stock of new company is held by voting trustees who vote it as directed by the commissioner. As I have also pointed out, the board of directors of new company are under the close supervision, control and direction of the commissioner and must, in reality, take orders from him as to every major, and some minor, business details. It cannot be said that this close supervision, control and direction exist in the usual "solvent" corporation.

Corporate Entity of New Company

Respondents argue that the corporate entity of new company cannot be disregarded so as to make the proposed mutualization a mutualization of old company. In support of this contention, *In re Bond & Mort. Guar. Corp.* 157 Misc. 240 [283 N.Y.S. 623, 652], and *Garrison* v. *Pacific Mut. L. Ins. Co.*, 83 Cal.App.2d 1, 9-10 [187 P.2d 893], are cited. In neither case was mutualization involved. In the Bond & Mortgage Guarantee case, the superintendent of insurance had organized Bond & Mortgage Guarantee *Corporation* "as a domestic insurance corporation, with a capital of $1,000,000, a surplus of $2,000,000, and a reserve for contingencies of $200,000, all of which was paid out of the assets of the guarantee *company* in exchange for the

BLEED THRU

entire capital stock of the new corporation, 10,000 shares of the par value of $100 each; a certificate for said number of shares was issued in the name of the guarantee *company* and is held by the superintendent of insurance as an asset, for the benefit of the creditors (including the policyholders), of the guarantee *company.*" (Emphasis added.) The guarantee corporation here involved took on the duty of insuring mortgages, "but on a restricted basis under a limited policy of guaranty." (Pp. 641, 650.) This case involved a proceeding whereby the People, and certain individuals interested, applied for an order enjoining the State Mortgage Commission from demanding and receiving or assuming control of certain mortgages being serviced by the guarantee *corporation* pursuant to court order. The injunction was granted. The contention was that the guarantee corporation, in servicing mortgages, was acting without adequate corporate powers. The court held that the corporation was acting within its corporate authority and, in answer to the contention that the guarantee corporation was a state agency inseparable from the superintendent of insurance (so as to permit another state agency, the Mortgage Commission, which came into being *after* the proceedings set forth had been had) to take it over, the court said:

"Said corporation is like any other corporation; a distinct entity. All of its stock is owned by guarantee *company*, and the certificate therefor is held in the custody of the superintendent; this he holds as he does any other assets of the company in rehabilitation, as a receiver designated by statute for the benefit of the creditors and stockholders of said company; not as an owner, representing the state. It is a stock corporation, having been created, for one thing, *with a view to its possible sale for the benefit of the creditors, as its exhaustive by-laws make apparent.* During such time as the stock control remains as it is, the operation of the corporation is to be under the supervision of the superintendent as rehabilitator." (Emphasis added.) The court continued and said that the primary management of the corporation was with the board of directors, although it was subject to the supervision of the superintendent "in his capacity as supervisor of insurance com-

DARK PA

panies" (pp. 651, 652). The situation presented in the New York case and that presented in the case at bar are factually similar up to a point. I have heretofore quoted extensively from *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 344, at page 356 [139 P.2d 908], where we set forth the extensive and minute supervision exercised by the commissioner over new company. This supervision exceeded by far anything required of him as "supervisor of insurance companies." We also said in *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal.2d 307, 324, 325 [74 P.2d 761], that new company was organized "as a corporate agent to assist him [commissioner] in carrying on the business of the old company." (See also *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 77, 80 [136 P.2d 779].)

In *Garrison* v. *Pacific Mut. L. Ins. Co.*, 83 Cal.App.2d 1 [187 P.2d 893], the court said, "The question for decision is whether an insurance company which was organized to conserve an insolvent insurance company and to rehabilitate its business is obligated to pay interest on claims allowed by the conservator against such insolvent, based upon the breach by the latter of certain policies, in the absence from the rehabilitation agreement of a specific promise to pay such interest, the agreement having provided for the payment to the liquidator for the benefit of such claimants an amount equal to the sum of all 'allowed claims' against the insolvent company." New company, by the terms of the rehabilitation agreement had agreed (Paragraph 17) "to pay to the liquidator for payment to claimants an amount equal to the sum of all claims against old company filed with the liquidator and finally allowed." The court answered the question put with this statement:

"It is customary practice in liquidation proceedings to marshal the assets of the debtor, fix the amount of its liabilities and disburse the assets among the creditors pro rata. Such a process would not be possible, if during the season of liquidation, the claims should be varied by the additions of varying amounts of interest." (P. 9). Respondents rely upon the following paragraph from the opinion of the District Court in the Garrison case: "Appellants contend that new company is a reincarnation of old

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company and, therefore, has impliedly promised to pay all of the latter's indebtedness. In this they ignore provisions of the Insurance Code, article 14 of chapter 1, part 2, division 1, which article deals with insolvency and liquidation proceedings under the article, *the commissioner may mutualize or reinsure the business of any person* affected by proceedings thereunder and may enter into rehabilitation agreements. *New company was organized by the sovereign power for the purpose of rehabilitating the business of one of its own creatures whose very existence inhered in the blood and sweat of the people.* It was to go forward under the guidance of the state. Its identity is utterly distinct from that of old company, notwithstanding the latter's equitable ownership of new company's stock. It cannot be fairly said that it is a continuance of old company. It did not take over the latter's assets or assume its burdens at the behest of old company. Such transfer and assumption were rendered indispensable to the public weal and were required by law to conserve the common good in general and the army of policyholders of old company in particular. New company was not organized by old company to do service in a prescribed manner for the latter but was created by the state to perform a public service. It must be ...d act in its own right upon the arena of trade and commerce and of human existence, free from the fetters of a collapsed institution which in the kaleidoscope of a changing world will soon be only a memory." (Pp. 9, 10.) New company was organized by the state to rehabilitate the business of old company; as the "corporate agent" of the insurance commissioner for that purpose. The language just quoted is, in part, illogical under the facts presented in this long line of litigation, including the Garrison case. It appears to me that the statement that "its [new company] identity is *utterly* distinct" is inconsistent with the latter part of the same sentence that this was so "notwithstanding the latter's [old company] equitable ownership of new company's stock" and with one of the preceding sentences wherein it is said that "New company was organized by the sovereign power for the purpose of rehabilitating the business of "old company, and the fact that new company "was

DARK PA

to go forward under the guidance of the state." The duties and obligations imposed upon the commissioner in this case amount to far more than his usual supervision of the usual solvent insurance company. There can be no doubt that new company is a separate *corporate* agency and that it was not organized by old company, but it does not logically follow that it is "utterly distinct" from old company. In my opinion, new company would have no existence but for the insolvency proceedings against old company. It also conclusively appears that the quoted statement from the Garrison case is dictum since it had nothing to do with the question involved there.

Respondents also argue that because this court said in *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal.2d 307, 334 [74 P.2d 761], that new company was, as a reinsurer, "substituted as an insurer in the place and stead of the original insurer" that the corporate identity of new company cannot be disregarded; that because this court said in the Carpenter case (p. 335) that "Every policyholder who consents to the Plan clearly enters into a novation with the New Company" that the two companies cannot be considered as "essentially one and the same." New company will in time replace old company but so long as old company exists *in any form*, it is clear that new company is still *only the corporate agent* of the commissioner for the purpose of rehabilitating the business of old company and that the mutualization plan must be worked out in accordance with the procedure provided for in that part of the Insurance Code relating to involuntary mutualization of insolvent companies. The stock of new company, held now by voting trustees, with beneficial ownership in the commissioner is still held by him for the benefit of the policyholders and creditors of old company. This fact cannot be disregarded; nor can the rights of the policyholders and creditors of old company be disregarded. In holding that new company is "utterly distinct" from old company for *all purposes*, a majority of this court chooses to forget *all the facts* concerning this litigation and pretends that new company was organized as any other insurance company with its own assets and liabilities, that the insurance

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commissioner had only the normal, nominal, supervision over its affairs, and that no insolvency proceedings had ever been involved. In the light of the record before us, such a holding cannot stand the test of honest scrutiny.

Res Judicata

Respondents argue that it has been decided by the superior court that the commissioner had authority to include in a rehabilitation agreement an option to mutualize the new company by voluntary proceedings and to agree to dispose of the stock of new company at the price, and on the terms, fixed by the price determination committee; and that this court has decided that the superior court had jurisdiction to so decide and that the superior court did not abuse its discretion in approving the rehabilitation agreement.

In the commissioner's answering brief (p. 61) is found this statement: "It is true that no attack seems to have been made on the mutualization provisions [of the rehabilitation agreement] in any of the appellate proceedings, but the courts have taken notice of them in determining various appeals." Neither this court, nor an appellate court, has been concerned in any of this litigation with the mutualization provisions of the rehabilitation agreement as will hereinafter appear.

In *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal.2d 307, 322 [74 P.2d 761], we said that the plan of rehabilitation provided for "Ultimate mutualization, in the event the policyholders so elect." We were there concerned in the main with the organization of new company as the corporate agent of the commissioner to rehabilitate the business of old company. In *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 13 Cal.2d 306 [89 P.2d 637], we were concerned with the validity of the "Order for Liquidation" and the mutualization provisions of the plan were not considered. In *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 14 Cal.2d 704 [96 P.2d 796], we were concerned with an order of the trial court correcting its minutes, *nunc pro tunc*. In *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 77 [136 P.2d 779],

DARK PA

we were concerned with the claims of dissenting policyholders and, once again, the mutualization provisions were not considered. In *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 344, 353 [139 P.2d 908], we were concerned with the propriety of creating a voting trust with the stock of new company under the provisions of section 1037, subdivision (e), of the Insurance Code. We said there that "To adopt the contention that section 1037(e) was not intended to apply to stock of an insurance company *organized as a medium through which rehabilitation of the business of a delinquent insurer was to be accomplished would require us to disregard the clear language of the statute.* Section 1037(e) specifically refers to stock issued to the commissioner 'as conservator or as liquidator in connection with a rehabilitation or reinsurance agreement.'" (Emphasis added.) We also said there (p. 355) that the rehabilitation agreement (Paragraph 20) related to the "ultimate status and ownership of the new company." We then pointed out that subdivision (a) (Paragraph 20) authorizes the commissioner to dispose of the stock in accordance with "any plan of mutualization thereafter adopted by the policyholders of the new company, and such a disposition may include a transfer to voting trustees if the plan of mutualization so provides." We held that the voting trust agreement was not a disposal of the stock within the meaning or purpose of Paragraph 20 of the rehabilitation agreement and we said (p. 358) that "It is true that the words 'dispose of' are used in subdivision (a) of paragraph 20 in connection with an authorization to the commissioner to transfer the stock of the new company to voting trustees in accordance with a plan of mutualization. *But it is clear that under that subdivision the transfer there provided for would require a complete alienation of the stock in order* to carry out the plan of mutualization contemplated therein." (Emphasis added.) Again, the validity of the mutualization procedure was not passed upon; the only holding being that the rehabilitation agreement did not preclude the creation of the voting trust. In *Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 386 [139 P.2d 930], we were concerned with disqualification of a judge and a party's waiver thereof. Mutualization was not consid-

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ered. In *Caminetti* v. *Pacific L. Ins. Co.*, 23 Cal.2d 94 [142 P.2d 741], we were concerned with the correctness of the measure of damages adopted by the commissioner to be allowed disability policyholders. In *Garrison* v. *Pacific Mut. L. Ins. Co.*, 83 Cal.App.2d 1 [187 P.2d 893], the court was concerned with the question of interest on claims allowed by the commissioner. In *Sanborn* v. *Pacific Mut. L. Ins. Co.*, 42 Cal.App.2d 99 [108 P.2d 458], the court pointed out that the following questions were involved: What was the effective date of the agreement between new company and the insurance commissioner as conservator of old company? Did appellant's present disability commence prior to such date and was notice of claim filed in accordance with the agreement?

It is contended by respondents, however, that a judgment upholding the validity of a contract establishes its validity, not only against the attacks actually made, but against those that could have been made, even though no question of invalidity was raised in the original proceeding and even though the judgment does not expressly pass on the contract.

Appellants argue that the procedure for mutualization provided for by statute cannot be altered by contract and that any attempt to do so is against public policy, illegal and void. It is true, of course, that the plan of mutualization, as proposed by the price determination committee, has never been before the courts until the present proceeding. The trial court, in its order of December 4, 1936, stated (13) "That said Rehabilitation and Reinsurance Agreement, and each and all of the terms and conditions thereof, and the plan therein embodied are, and each of them is, hereby approved; . . ." (Clk. Tr., p. 169.) This was an approval *only* of the agreement and, while grossly wrong, does not now preclude this court from correcting the error since the *plan* of *mutualization* was not passed upon *nor could it have been* since it was to be promulgated *10* years in the future.

We said in the Caminetti case (22 Cal.2d 344, 363) "This proceeding is wholly statutory. The duties imposed upon

DARK PA

the commissioner, and the supervision over him vested in the courts, result from the statute." Appellants, citing *Fortenbury* v. *Superior Court*, 16 Cal.2d 405, 407-408 [106 P.2d 411], contend that if the order of the trial court (December 4, 1936) is considered as having approved a plan of mutualization contrary to the statutory provisions therefor, it is void for want of jurisdiction of the subject matter. The respondents' position is that this court having previously determined the trial court's jurisdiction, the matter is res judicata. In the Fortenbury case, we said "The term jurisdiction originally included only the right to hear and determine concerning the subject matter in a particular case. But the modern tendency has been to broaden the meaning, particularly where the right to review a decision by certiorari, or other prerogative writ is the question for decision. *A court may have jurisdiction of the cause of action and of the parties, but it may lack the authority or power to act in the case except in a particular way.* Under such circumstances, it is now generally held that the court had no jurisdiction. As pointed out in the case of *Spreckels S. Co.* v. *Industrial Acc. Com.*, 186 Cal. 256, 260 [199 P. 8], 'the word is frequently used as meaning authority to do the particular thing done, or, putting it conversely, a want of jurisdiction frequently means a want of authority to exercise in a particular manner a power which the board or tribunal has, the doing in excess of the authority possessed.' " (Emphasis added.) We also said in *First Industrial Loan Co.* v. *Daugherty*, 26 Cal.2d 545, 556 [159 P.2d 921], that "It is elementary that power given to the Commissioner of Corporations (by section 10 of the act) 'to establish such rules and regulations as may be reasonable or necessary to carry out the purposes and provisions of this act' *does not include power to alter the statute or enlarge or impair its scope.*" (Emphasis added.)

It seems apparent that if the involuntary mutualization provisions for insolvent insurance companies are applicable the commissioner was acting without statutory authority in approving a plan of mutualization based upon the statutory provisions relating to voluntary mutualization of solvent companies and that his approval thereof was void,

BLEED THRU

as was his agreement to approve such a plan. The rule is settled that a contract in violation of an express statutory provision is void and that it is not necessary that the statute expressly so declare (*City of Oakland* v. *California Const. Co.*, 15 Cal.2d 573, 576 [104 P.2d 30]). A contract made in any manner except that expressly provided in the applicable statute is ipso facto void (*Dale* v. *Palmer*, 106 Cal.App.2d 663, 667 [235 P.2d 650]). If upon review of all the legislation on the subject the contract appears to contravene the design and policy of the laws, the courts will not enforce it (*Kreamer* v. *Earl*, 91 Cal. 112 [27 P. 735]; *Loew's Inc.* v. *Cole*, 185 F.2d 641). See *Hill* v. *Bank of San Pedro*, 41 Cal.App.2d 595, 607 [107 P.2d 399]; *County of San Diego* v. *California Water etc. Co.*, 30 Cal.2d 817 [186 P.2d 124, 175 A.L.R. 747]; *Film Producers, Inc.* v. *Jordan*, 171 Cal. 664 [154 P. 605].

The parties are in disagreement as to whether or not the mutualization provisions were litigated at the time the order of December 4, 1936, was made. The insurance commissioner says that "*Presumably* these provisions did not go entirely unchallenged in the proceedings leading up to the Order of Rehabilitation." (Emphasis added.) (Insurance commissioner's answering brief, p. 61.) New company asserts that the "validity" of the rehabilitation agreement was put in issue and decided by the order of December 4, 1936, and that the same has been approved by this court. From all that appears, it is obvious that the precise question here involved has never been passed upon. It most certainly has not been passed upon by an appellate court, or by this court. Respondent, new company, points to the following quotations from the pleadings in the original proceeding as showing that the mutualization provisions of paragraph 20(a) were litigated. "Answer of Certain Interveners to Petition for Approval of Second Proposed Rehabilitation and Reinsurance Agreement, Folios 2757-2759 of Transcript on Appeal. L. A. 16182:

"That said plan, if executed, would be entirely void and of no effect, and would not be binding upon the parties thereto, and that the execution of the same is beyond the authority of the said Samuel L. Carpenter, Jr., as Insur-

DARK PA

ance Commissioner of the State of California and as Conservator of The Pacific Mutual Life Insurance Company of California [old company], and that the execution of said agreement and the transfer of the assets by the said Insurance Commissioner is wholly unauthorized by the Insurance Code of the state of California and is entirely beyond the power of the said Samuel L. Carpenter, Jr., as Insurance Commissioner and as Conservator as aforesaid, and the said agreement will be void when executed and beyond the power of the Insurance Commissioner under the statute in such cases made and provided and that the said agreement is of no binding effect whatever on any of the parties thereto and that any acts done pursuant thereto are wholly null and void."

"Amended Complaint in Intervention of Certain Intervenors, Folio 3882 of Transcript on Appeal, L.A. 16182:

"That the approval of said agreement is beyond the authority and jurisdiction of this court and, if given, would be void and of no force and effect, for the reason that authority therefor is not given in, and, in fact, is forbidden by, the terms and provisions of said Insurance Code of California, and, in particular, of articles is [sic] and 14 of chapter 1 of part 2 of division 1 thereof."

It appears to me that what was undoubtedly meant by these pleadings was that the *organization* of *new company* was said to be beyond the commissioner's power since that was the major issue in *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal.2d 307 [74 P.2d 761].

The next question that arises is whether or not the provisions for mutualization *could* have been litigated in that proceeding inasmuch as mutualization was not to take place until between 1946 and 1948, or "so long as the Conservator or a Liquidator of the Old Company may continue to hold any or all of said stock. . . ." (Paragraph 20(a), rehabilitation agreement.) The proposed voluntary mutualization plan was also to be in accordance "with the laws of the State of California in effect at the time of said request. . . ." The plan was also not to be proposed unless the price determination committee "shall determine whether in their

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opinion the proposed voluntary mutualization of the New Company . . . can then be practicably accomplished. . . ." In *Silva* v. *City & County of San Francisco,* 87 Cal.App.2d 784 [198 P.2d 78], a county board of supervisors passed a resolution that certain land of plaintiff's should be acquired when necessary. Plaintiff sued for a declaration as to the value of his property. The court, in refusing to place plaintiff's valuation on the property, declared: "The court may take judicial knowledge that real estate values do not remain constant. The value fixed during the present period may be disproportionate to what should be paid when the recreation department of the city decides to use the property as part of a 'playground.' Plaintiff seeks a final determination that the property is worth $10,000 and that *if* and *when* defendant chooses to take the property this will be the amount it must pay." (Emphasis that of the court.) It was also said that ". . . the present complaint alleges in substance that the value of the property may be determined through condemnation proceedings when defendant deems it 'necessary.' The only declaratory judgment that could be rendered under the allegations of the complaint would be of an advisory nature—namely, that when defendant deems it necessary to institute condemnation proceedings the price be fixed at the then market value." (Pp. 788-789.)

In *Young* v. *Young,* 100 Cal.App.2d 85, 87 [223 P.2d 25], it was held that an action to establish a foreign decree of divorce in California, and for ratification by the California court of a property settlement included in the foreign decree, did not present a justiciable controversy in the absence of a showing that defendant had refused or failed to comply with the foreign decree or the terms of the property settlement agreement. It was held that "The rule is accurately stated in 1 California Jurisrudence (1921) at page 335, section 25, as follows: 'To invoke the jurisdiction of a court of justice, it is primarily essential that there be involved a genuine and existing controversy, calling for present adjudication as involving present rights.' (See also *Neill* v. *Five C. Refining Co.,* 79 Cal.App.2d 191 [179 P.2d 818]), wherein Mr. Justice Drapeau thus pointedly states the rule at page 193, 'An action not founded upon an ac-

DARK PAGE

tual controversy, or prosecuted "for the gratification of the curiosity of the litigants" is collusive and will not be entertained. [Citing cases.]' "

In *Merkley* v. *Merkley*, 12 Cal.2d 543, 547 [86 P.2d 89], the court stated that "The facts in the record present an academic question only. The courts will not exercise the discretionary power to declare rights which do not give rise to a present controversy."

In *County of San Diego* v. *California Water etc. Co.*, 30 Cal.2d 817, 823, 826 [186 P.2d 124, 175 A.L.R. 747], a case involving an agreement by a county to relocate a county highway, we enunciated the following rule: That if the Legislature had provided a method by which a county or city might abandon or vacate roads, that method was *exclusive*. We said: "It is clear, however, that neither the doctrine of estoppel nor any other equitable principle may be invoked against a governmental body where it would operate to defeat the effective operation of a policy adopted to protect the public. (See *Miller* v. *McKinnon*, 20 Cal.2d 83 [124 P.2d 34, 140 A.L.R. 570], and cases cited therein; *Pan Amer. Co.* v. *United States*, 273 U.S. 456, 505-506 [47 S.Ct. 416, 71 L.Ed. 734]; *American Surety Co. of N. Y.* v. *United States* (C.C.A. 10th), 112 F.2d 903, 906.) In the American Surety Company case the court stated that the government could not be estopped so as to 'frustrate the purpose of its laws or thwart its public policy.' (112 F.2d, at p. 906.) In 3 McQuillin, Municipal Corporations [2d ed., 1943], section 1266, it is said that various statutory procedures or steps exist to protect citizens and taxpayers from ill-considered contracts or those showing favoritism and that if recovery is allowed for property or services on the ground of estoppel or implied contract, 'then it follows as the night the day that the statute or charter provision can always be evaded and set at naught.' The author adds that the rule denying indirect enforcement of such void contracts harmonizes with our governmental system, appears to be supported by reason, and is not unjust, because the other party is charged with notice of the law."

At any rate, the *plan* of mutualization, as distinguished from the *provisions* for mutualization as found in the re-

BLEED THRU

habilitation agreement, has never until this case, been passed upon. That plan, while following the outline contained in Paragraph 20(a) made some 10 years prior to the promulgation of the one here under consideration, is an entirely different matter and may properly be held void as not in accordance with the statutory scheme for involuntary mutualization of insolvent insurance companies seized by the commissioner under the provisions of sections 1010 and 1011 of the Insurance Code. The rule enunciated in *County of San Diego* v. *California Water etc. Co., supra,* hereinabove set forth would be applicable if the plan of mutualization is held void as against public policy and as being in excess of the commissioner's jurisdiction.

It should be noted that Paragraph 20(f) contains a provision to the effect that if all, or any part, of the paragraph should be contrary to law, or illegal, or void, the vulnerable provision should be deemed separable and the balance of the agreement should stand. If, as I believe, the validity of Paragraph 20(a) has never been before determined, the provision just noted would prevent anything that has been heretofore determined by either this court, or any appellate court, from conflicting with the determination made here.

Trial De Novo

If the procedure for involuntary mutualization had been followed, as it should have been, this question would never have arisen. Section 1048 of the Insurance Code provides that after the formulation of the mutualization plan, it "shall" be submitted by the commissioner to the court for its approval. The clear import of the procedure outlined for insolvent organizations is that those possessed of property rights in them must be accorded *court* protection at *every* stage. For example, the *court* appoints the appraisers (§ 1051). Such court approval, required by section 1048, accords the interested parties the equivalent of a trial de novo.

According to the majority opinion, the "alternative" reason given for affirmance is reliance upon the doctrine of res judicata. That this reason is patently false is shown

by Mr. Justice Traynor when he points out that the court "could obviously not approve [the] plan at the time it entered its order approving the rehabilitation agreement. Moreover, it did not expressly approve in advance the carrying out of any mutualization plan that might be presented by the price determination committee." He shows that there is reserved to the court, by the agreement, continuing jurisdiction to approve or disapprove plans to be developed in the future for mutualization or other disposal of the stock in the hands of the commissioner. He points out that to so interpret the order subserves the primary purpose of section 1037, subdivision (d), of the Insurance Code by securing to all interested parties "their right to court scrutiny." Appellants have not been accorded "court scrutiny" in its true sense.

Appellants correctly contend that the order of the commissioner approving the plan of mutualization was subject to full judicial review by the superior court. It is argued that the commissioner, in making his order, acted in a judicial capacity rather than in an administrative or legislative capacity as contended by respondents. Appellants contend that in reviewing a decision or order of a statewide administrative agency or of a state officer, the superior court must reweigh the evidence and determine for itself according to its independent judgment whether or not the decision is supported by the weight or preponderance of the evidence in every case where state judicial functions are involved. They rely upon *Thomas* v. *California Emp. Stab. Com.*, 39 Cal.2d 501, 504 [247 P.2d 561]; *Moran* v. *Board of Medical Examiners*, 32 Cal.2d 301, 308 [196 P.2d 20]; *Laisne* v. *California State Board of Optometry*, 19 Cal.2d 831, 834-835 [123 P.2d 457]; and *Drummey* v. *State Board of Funeral Directors & Embalmers*, 13 Cal.2d 75 [87 P.2d 848]. Respondents, on the other hand, argue that the commissioner's order was an exercise of executive power and was not the exercise of such full judicial power as to entitle appellants to have the trial court exercise its independent judgment with respect to the weight of the evidence. Respondents rely upon the cases of *Bank of Italy* v. *Johnson*, 200 Cal. 1 [251 P. 784]; *Doble Steam Mo-*

tors Corp. v. *Daugherty,* 195 Cal. 158 [232 P. 140]; *McDonough* v. *Goodcell,* 13 Cal.2d 741 [91 P.2d 1035, 123 A.L.R. 1205], and *Southern Calif. Jockey Club, Inc.* v. *California etc. Racing Board,* 36 Cal.2d 167 [223 P.2d 1].

The duties of the commissioner, as set forth in section 12921 have been held to be "that of a minister of the court in possession of the property, to the end of conserving the rights of everybody having any interest" (*H. D. Roosen Co.* v. *Pacific Radio Pub. Co.,* 123 Cal.App. 525 [11 P.2d 873]) and discretionary (*Garris* v. *Carpenter,* 33 Cal.App. 2d 649, 657 [92 P.2d 688]). It was held in *Caminetti* v. *Guaranty Union Life Ins. Co.,* 22 Cal.2d 759, 764 [141 P.2d 423], that the commissioner's ". . . office is not to perform functions in aid of the court's jurisdiction to decide a controversy between litigants, but he acts as a statutory officer, subject however to judicial supervision to prevent an arbitrary exercise of power on neglect of duty." The court in the Caminetti case, however, was referring to the commissioner as a receiver of the assets of insurance companies and stated that he did not derive his power from the court, but from the statute.

The distinction in the two lines of cases relied upon by appellants and respondents is that in those relied upon by appellants an existing vested property right was extinguished, or taken away, by the administrative order. For example, in the Drummey case (13 Cal.2d 75) Drummey and Wilson had been duly licensed embalmers and the State Board of Funeral Directors and Embalmers ordered their licenses suspended. This court held that it was dealing with a statute which conferred certain fact-finding powers on a board exercising statewide jurisdiction and that there was no "indication that the legislature intended the facts so found to be binding on the courts"; that no method of review was provided in the statute. We held that we could see no escape from the conclusion that in such a proceeding the court to which the application for mandate is made must weigh the evidence, and exercise its independent judgment on the facts as well as the law, if the complaining party is to be accorded his constitutional rights under the state and federal Constitutions. "The

state constitutional provision discussed, *supra*, prohibits the conferring of judicial power on such administrative boards" (p. 84).

In *Laisne* v. *California State Board of Optometry, supra*, the California State Board of Optometry had revoked Laisne's certificate of registration to practice optometry in this state. We held there that "On the authority of the Drummey case the only type of review that would afford appellant his full constitutional rights would be a complete trial de novo as outlined in the decision in that case." (P. 843.)

In *Moran* v. *Board of Medical Examiners, supra*, the State Board of Medical Examiners revoked the license of Dr. Moran to practice medicine in this state. We held "That the trial court in this case was 'authorized by law to exercise its independent judgment on the evidence' is well established. (See *Dare* v. *Board of Medical Examiners* (1943), 21 Cal.2d 790, 795 [136 P.2d 304]; *Sipper* v. *Urban* (1943), 22 Cal.2d 138, 141 [137 P.2d 425]; *Hohreiter* v. *Garrison* (1947), 81 Cal.App.2d 384, 402 [184 P.2d 323].) As stated in the last cited case, at page 402, 'Thus, the ultimate power of decision rests with the trial court.'" (P. 308.)

In *Thomas* v. *California Emp. Stab. Com.*, 39 Cal.2d 501 [247 P.2d 561], it was held that unemployment benefits provided for by the Unemployment Insurance Act were such property rights as to fall within the rule that persons deprived of property rights by a statutory administrative agency were entitled to a limited trial de novo in the superior court.

Respondents' positions (which has been adopted in toto by the majority opinion) is that the "Order" of the commissioner was merely a "permit" which allowed mutualization if the policyholders so voted. (§ 11526, subd. (d)) and that the order did not deprive anyone of vested property rights. We have heretofore held (*Thomas* v. *California Emp. Stab. Com.*, 39 Cal.2d 501, 504 [247 P.2d 561]; *Laisne* v. *California State Board of Optometry*, 19 Cal.2d 831 [123 P.2d 457]; *Moran* v. *Board of Medical Examiners*,

32 Cal. 2d 301, 308 [196 P.2d 20]; *Drummey* v. *State Board of Funeral Directors & Embalmers*, 13 Cal.2d 75 [87 P.2d 848]) that where an existing property right is extinguished by the questioned administrative order the one so deprived is entitled to a trial de novo in the superior court. Appellants here are the beneficial owners of the stock of the new company which is held by the voting trustees for their benefit. Under the proposed mutualization plan, this stock will be nonexistent and they will be forced to accept a price therefor, as well as terms, over which they have exercised no control. Mr. Justice Traynor has pointed out that if the proper procedure had been followed, the rights of these people would have been protected by a court of law, rather than subjected to the action of one man acting in three irreconcilable positions. The assets of old company were transferred to new company in exchange for all the stock of new company which, in the beginning, was held by the commissioner, as conservator for the benefit of the creditors, policyholders, and stockholders of old company (*Caminetti* v. *Pacific Mut. L. Ins. Co.*, 22 Cal.2d 344, 351 [139 P.2d 908]). Later, the stock of new company was transferred to voting trustees who held legal title thereto, ". . . with the power to exercise all the rights of ownership. The commissioner, however, retains the entire beneficial interest for the benefit of creditors of the old company and others interested." (22 Cal.2d. at page 357.) As stated by the insurance commissioner in his opinion and decision (page 7 of the exhibit): "Greatly epitomized, the plan [of mutualization] determined that both the Participating and Non-Participating Life Departments of the company should be mutualized by the *purchase and cancellation of all of the outstanding shares of capital stock of the New Company*, thus converting the New Company into a non-stock insurer conducted for the benefit of its members who shall be the policyholders of the participating and non-participating life classes." Inasmuch as purchase and cancellation of the stock of new company will be accomplished by the proposed mutualization, it appears that appellants have been deprived, by the order, of their vested beneficial ownership of that stock so as to entitle them to a trial de novo within the rule of the cited cases.

DARK PAGE

The majority opinion states: "The approval of the mutualization plan by the commissioner did not involve any deprivation of property rights or vested rights; it was in essence a permit or license authorizing the new company to purchase its own stock." This *would* be true *if* new company members owned their own stock (and therein lies the fallacy in calling new company a solvent corporation with all that term connotes). But the matter is not quite so simple. All the beneficial ownership, which is the *real* ownership is held by the policyholders and stockholders of old company; all the legal title is held by the voting trustees (appointed by the commissioner) for the benefit of *old company* policyholders and stockholders. In other words, new company holds neither legal nor beneficial ownership of its stock, but through the medium of the mutualization plan is given the right to deprive the beneficial owners of their property in clear violation of the law as heretofore propounded by this court. We held in the Drummey case that we could see no escape from the conclusion that the court must weigh the evidence and exercise its independent judgment on the facts as well as the law, if the complaining party was to be accorded his *constitutional rights* under the state and federal Constitutions. "The state constitutional provision discussed, *supra,* prohibits the conferring of judicial power on such administrative boards."

In *St. Joseph Stock Yards Co.* v. *United States,* 298 U.S. 38, 52 [56 S.Ct. 720, 80 L.Ed. 1033], the court stated: "Legislative agencies, with varying qualifications, work in a field peculiarly exposed to political demands. Some may be expert and impartial, others subservient. It is not difficult for them to observe the requirements of law in giving a hearing and receiving evidence. But to say that their findings of fact may be made conclusive *where constitutional rights of liberty and property are involved,* although the evidence clearly establishes that the findings are wrong and *constitutional rights have been invaded,* is to place those rights at the mercy of administrative officials and seriously to impair the security inherent in our judicial safeguards. That prospect, with our multiplication of administrative agencies, is not one to be lightly regarded.

LEED THRU

It is said that we can retain judicial authority to examine the weight of evidence when the question concerns the right of personal liberty. But if this be so, it is not because we are privileged to perform our judicial duty in that case and for reasons of convenience to disregard it in others. *The principle applies when rights either of persons or of property are protected by constitutional restrictions.* Under our system there is no warrant for the view that the judicial power of a competent court can be circumscribed by any legislative arrangement designed to give effect to administrative action going beyond the limits of constitutional authority." (Emphasis added.) This case and this statement were relied upon by us in the Drummey case (*supra*, 13 Cal.2d 75, 85) and no information has been presented to me to show that the rule there set forth has been in any way changed. No clearer case than this could possibly be found to illustrate the evils to be avoided. Old company stockholders and policyholders have been, and are, at the "mercy" of administrative officials; those officials may, during the last 10 years, have been either "expert and impartial" or "subservient."

I have heretofore set forth at length the self-evident fact that appellants are possessed of vested property rights of which they are being deprived. In *Ohio Valley Water Co.* v. *Ben Avon Borough*, 253 U.S. 287, 289 [40 S.Ct. 527, 64 L.Ed. 908], it was held: "The order here involved prescribed a complete schedule of maximum future rates and was legislative in character. *Prentis* v. *Atlantic Coast Line R. Co.*, 211 U.S. 210 [29 S.Ct. 67, 53 L.Ed. 150] *Lake Erie & W. R. Co.* v. *State Public Utilities Com.*, 249 U.S. 422, 424 [39 S.Ct. 345, 63 L.Ed. 684]. In all such cases, *if the owner claims confiscation of his property will result, the state must provide a fair opportunity for submitting that issue to a judicial tribunal for determination upon its own independent judgment as to both law and facts: otherwise the order is void because in conflict with the due process clause, fourteenth amendment. Missouri Pac. Ry. Co.* v. *Tucker*, 230 U.S. 340, 347 [33 S.Ct. 961, 57 L.Ed. 1507]; *Wadley Southern Ry. Co.* v. *Georgia*, 235 U.S. 651, 660, 661 [35 S.Ct. 214, 59 L.Ed. 405]; *Missouri* v. *Chicago, B. & Q. R. Co.*, 241 U.S. 533, 538 [36 S.Ct. 715, 60

L.Ed. 1148]; *Oklahoma Operating Co.* v. *Love*, 252 U.S. 331 [40 S.Ct. 338, 64 L.Ed. 596]." (Emphasis added.)

Appellants here complain bitterly because the mutualization plan provides that the price to be paid for new company's stock (of which they are the *beneficial owners*) is $3,000,000 while that same amount was originally taken out of old company's funds to purchase new company's stock and, *in addition*, all the other assets of old company (over $200,000,000 in assets plus such intangibles as going agency organization and concern, good will, etc., "worth several millions of dollars" [*Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal.2d 307, 325 (74 P.2d 761)]) were turned over to new company! It surely must be crystal clear to everyone who can think that such an outrageous confiscation of property without due process of law has never before taken place in this state.

Evidence

In the trial court the evidence consisted of all of the record of the proceedings before the insurance commissioner, consisting of the reporter's daily transcript, the exhibits and the commissioner's decision. Appellants contend that they were prohibited from introducing evidence, or offering to do so, because of the rulings of the trial court; that no issues of fact were litigated; that the court ruled that it was not empowered to exercise its independent judgment on the evidence taken before the commissioner. Respondents state that appellants were given leave to serve and file a motion and affidavits relative to the introduction of additional evidence and failed to do so. The memorandum opinion and order (July 2, 1951, Clk. Tr., 237-239) contains this statement: "After a careful study of the briefs submitted and the authorities cited I have come to the conclusion that, so far as any matter of fact is concerned, this Court is limited to determining whether or not the findings of the Commissioner are *supported by substantial evidence in the light of the whole record, but that it is for this court to exercise its independent judgment in interpreting the Rehabilitation Agreement and in construing and applying section 11527* of the Insurance Code. . . .

"I have come to the further conclusion that this Court cannot receive any additional evidence, but that upon proper showing may remand this matter to the Commissioner to take further evidence and reconsider the case in the light of such evidence. . . ."

Appellants point to the statements made by the trial judge on the settlement of findings that "*I think it must be very evident if I had had this case to decide on a new question of fact my decision might have been the opposite*" (emphasis added; page 766, Rep. Tr.) and "It [fixing the price] is very complex, and I think you are making it more complex. My finding was, and the basis of my determination was that they [the price determination committee] had a reasoned basis in fixing the price. That is the fact. If they had acted unreasonably then I would have had to set it aside. It was only because I could not convince myself that it was not a rational conclusion that they acted upon that I ever decided the case the way I did. *Because I could not take the facts and arrive at the same conclusion; not by a long shot. But because I did not feel that I could substitute my opinion for theirs, or substitute my opinion for the Commissioner's, that is the reason I arrived at the conclusion that I did.* But that is the crux of it. It is not the details that they took in. What you are entitled to find now is entirely evidentiary." (Emphasis added.) The inference from this is obvious—that had the involuntary procedure been followed, the court would have withheld its approval because the plan did not protect the interests of those owning the beneficial interests.

The just-quoted statement made by the trial court shows, without equivocation, that had there been a trial de novo his decision would have been contrary to that reached. His statement shows that he was convinced that the weight of the evidence was with appellants but, believing himself limited by the substantial evidence rule, his conclusion was in favor of respondents. The only rational conclusion to be drawn from the facts of this case is that appellants were possessed of a vested property right and, therefore, should have been given a trial de novo in a *judicial tribunal*

provided by the state for the protection of private property rights. Because appellants were not afforded a trial de novo they have been deprived of their property without the due process of law guaranteed to them by both the state and federal Constitutions.

Summary of Major Points

(1) It is my opinion that the provisions of the Insurance Code relating to voluntary mutualization of solvent insurance companies were not applicable to new company. As I have heretofore pointed out, new company was organized because of the insolvency of old company and cannot be considered as a solvent company until the liabilities arising from the non-can policies have been paid or sufficient funds accumulated to pay them. The voluntary mutualization provisions of the code in and of themselves show that they were intended by the Legislature to apply to not only a *solvent* company but to a company not so closely supervised by the commissioner as the one here under consideration. The ordinary solvent company is not such a hybrid as we have in new company. In using the voluntary procedure, we have the commissioner, acting as conservator and beneficial owner of the stock of new company, agreeing to vote for the plan of mutualization as proposed by the price determination committee. As conservator, and beneficial owner of the stock of new company, he is *supposed* to be protecting the rights and interests of those in the position of appellants. When, as commissioner, he approves the proposed plan as fair and equitable, under the voluntary mutualization procedure, he is concerned with the fairness of the plan as it concerns those interested in new company. If the normal solvent company were being mutualized, the plan of mutualization would be proposed by the company itself, approved by its board of directors, adopted by a majority vote of its own shareholders, and then approved by the commissioner who, presumably, would not have seen the plan, or even heard of it, prior to the time it was presented to him for his approval as fair and equitable to those concerned—the shareholders and policyholders of the solvent company.

The following statement is found in the majority opinion: "In numerous cases where the action of an administrative officer was necessary *to prevent defeat of the statutory scheme*, his participation has been upheld although the grounds for disqualification were much more serious than those raised here." (Emphasis added.) The author again assumes too much. He assumes that the "statutory scheme" was being carried out. On the contrary, the statutory scheme is being *defeated*. The entire scheme for rehabilitation of insolvent corporations, and the statutory protection of the interested persons therein, is abrogated through the use of the procedure designed for mutualization of solvent corporations.

(2) I am also of the opinion that Paragraph 20(a) of the rehabilitation agreement has never before been judicially determined and, therefore, its provisions are not res judicata of the present controversy. I have pointed out that there is a separability clause in the rehabilitation agreement and that nothing heretofore done by this, or an appellate court, will be affected by a holding by this court that the parties may not validly contract to mutualize new company contrary to the applicable statutory provisions.

(3) There should have been a trial de novo in the superior court where evidence relative to the proper method to be used by the price determination committee, or *court-appointed* appraisers, could have been introduced by both sides and a determination made by a judicial trier of fact. Both appellants and respondents here devote many pages of their numerous briefs to such material. Such methods are obviously matters for experts in the field of insurance and should be the subject of testimony in the trial court.

(4) If, as I firmly believe, the procedure for involuntary mutualization of insolvent companies is the proper procedure, sections 1049, 1050, 1051 and 1052 of the Insurance Code contain detailed provisions for hearings and the appointment by the court of appraisers to appraise "the then outstanding shares of the capital stock of such insurer, without regard to any appreciation or depreciation arising out of said mutualization plan as so approved or modified.

Such appraisement shall fix the reasonable value of such shares of capital stock, including the goodwill, if any, of such insurer, and shall state the value, if any, assigned to such goodwill; and if the appraisers shall have found that such insurer has no goodwill, such finding shall be stated. Such appraisement, when confirmed by said court, shall be final and conclusive." (§ 1051.)

The use of the involuntary mutualization procedure for an insolvent company follows logically from the original proceeding under sections 1010 and 1011. It should be noted that section 1054 (still under the Insolvency and Delinquency sections) provides that: "*Such insurer, after mutualization, shall be a continuation of the original insurer, and such mutualization shall not affect existing suits, rights or contracts except as provided in said mutualization plan as approved.* Such insurer, after mutualization, shall exercise all the rights and powers and perform all the duties conferred or imposed by law upon insurers writing the classes of insurance written by it, and to protect rights and contracts existing prior to mutualization, subject to the effect of said mutualization plan." (Emphasis added.)

We held in *Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal.2d 307, 334 [74 P.2d 761], that "reinsurance" was a contract by which one company (new company) takes over the insurance risks of another company (old company) and becomes substituted as an insurer in the place and stead of the original insurer. This holding is also the logical result of following the procedure outlined in the Insolvency and Delinquency division of the Insurance Code.

From what Mr. Justice Traynor has said in his dissent and from the reasons heretofore set forth by me, the conclusion is *inescapable* that the judgment should be reversed.

SCHAUER, J.—I concur generally in the discussion, the reasoning and the conclusions of Mr. Justice Carter.

APPENDIX B.

Opinion of the District Court of Appeal.

[Civ. No. 15977. First Dist., Div. Two. May 14, 1954 (as modified June 11, 1954).]

The Pacific Mutual Life Insurance Company (a corporation) *et al.*, appellants, v. John R. Maloney, as Insurance Commissioner, etc., *et al.*, respondents.

Appeal from a judgment of the Superior Court of Los Angeles County. Paul Nourse, Judge. Affirmed.

Proceeding in mandamus to rescind order of Insurance Commisioner approving plan to mutualize an insurance company. Judgment denying writ affirmed.

Joseph L. Lewinson and Henry W. Low for appellants.

C. Ray Robinson and William B. Boone, as Amici Curiae on behalf of appellants.

O'Melveny & Myers, Paul Fussell, Homer I. Mitchell, James E. Cross, George B. Gose, Frank P. Doherty, Guy Knupp and Peery Price for respondents.

Lloyd W. Dinkelspiel and Heller, Ehrman, White & McAuliffe, as Amici Curiae on behalf of respondents.

GIBSON (Lilburn), *J. pro tem.**—This is an appeal from a judgment of the Superior Court, which denied a peremptory writ of mandate and discharged an alternative writ previously issued.

The peremptory writ was sought under the provisions of Section 1094.5 of the Code of Civil Procedure to rescind an order of the Insurance Commissioner approving a plan to mutualize Pacific Mutual Life Insurance Company, a California corporation (referred to hereinafter as "New Company").

The alternative writ discharged by the judgment included an order staying the execution of the Plan of Mutualization. By stipulation a stay order was made by the

* Assigned by Chairman of Judicial Council.

DARK PAGE

District Court of Appeal, Second Appellate District, Division Three, prior to the expiration of the stay order made by the Superior Court. The stay order made by such appellate court is now in force.

The Plan of Mutualization was submitted to Honorable Wallace K. Downey as Insurance Commissioner in his character as an administrative officer, purportedly in pursuance to the provisions of subdivision (c) of Section 11526 of the Insurance Code (relating to the mutualization of nondelinquent stock companies), which provides that such a Plan of Mutualization must be approved by the board of directors of a company and its stockholders, and the Insurance Commissioner.

Order approving the plan was made after a hearing under Section 11527 of the Insurance Code, which provides:

"The commissioner shall examine the plans submitted to him under the provisions of subdivision (c) of Section 11526. He shall not approve such plan unless in his opinion the rights and interests of the insurer, its policyholders and shareholders are protected nor unless he is satisfied that the plan will be fair and equitable in its operation."

After the conclusion of the hearing Mr. Downey, as commissioner, made affirmative findings in accordance with the provisions of the section, and approved the Plan of Mutualization.

The petition for mandate alleges that the order of the insurance commissioner was made without jurisdiction and was not justified by the evidence.

Appellants, who were petitioners below (sometimes referred to herein as petitioners), are The Pacific Mutual Life Insurance Company of California, a California corporation (referred to hereinafter as "Old Company"), and Samuel K. Rindge, and others, who are stockholders in the Old Company, and the members of Pacific Mutual Shareholders Protective Committee.

In the receivership proceedings Honorable Samuel L. Carpenter, Jr., Insurance Commissioner of the State of

BLEED THRU

California, first acted as conservator and then as liquidator of the Old Company, and several successors as Insurance Commissioners, including Honorable John R. Maloney, have acted as liquidator and Mr. Maloney now acts as liquidator.

Respondents below and here are the New Company and Mr. Maloney, as Insurance Commissioner of the State of California and as liquidator of the Old Company.

The order approving the Plan of Mutualization was made by Mr. Downey on September 22, 1950, at the time he was Insurance Commissioner of California and liquidator of the Old Company. He was named in the petition for mandate as a respondent, both in his character as Insurance Commissioner and as liquidator; but during the pendency of the proceeding in mandate, Mr. Downey was succeeded in both capacities by Mr. Maloney, and Mr. Maloney was accordingly substituted for Mr. Downey and the cause proceeded against Mr. Maloney in both capacities.

In 1936 The Pacific Mutual Life Insurance Company of California was in the possession of the Insurance Commissioner as conservator by reason of its insolvency. On December 4, 1936, by order of the court in the proceedings for the conservatorship of Old Company, title to all of the outstanding capital stock of New Company was vested in the Insurance Commissioner, as conservator of Old Company, subject to an option in favor of the participating life policyholders of New Company, giving them the right, after the expiration of approximately 10 years, to institute mutualization proceedings, that is, proceedings to cause New Company to purchase its capital stock for the purpose of converting the company from a stock company to a mutual company. Such option was contained in the rehabilitation and reinsurance agreement under the terms of which the business of Old Company was rehabilitated by organizing a new and solvent company, which acquired most of the assets and assumed most of the liabilities of Old Company. The rehabilitation and reinsurance agreement is the source and basis of appellants' claim

to the equitable interest in the proceeds of any sale of New Company stock that might be made by the Insurance Commissioner as liquidator (formerly conservator) of Old Company.

The rehabilitation and reinsurance agreement is also the source and basis of the right of the participating life policyholders of New Company to cause the company to acquire its stock (and thus accomplish its mutualization) at such price and upon such terms as might be fixed by a price determination committee, to be selected by the president of Stanford University, the provost of the University of California at Los Angeles, and the president of the Association of Life Insurance Presidents (the name of which was later changed to Life Insurance Association of America). That agreement, including the option in favor of the participating life policyholders of New Company, was, with the approval of Judge Henry M. Willis, after a hearing in the proceedings for the conservatorship of Old Company, executed by the conservator and by New Company. Judge Willis's order of approval, dated December 4, 1936, adjudged that the rehabilitation and reinsurance agreement was valid. Appeals were taken and the judgment was affirmed. (Carpenter v. Pacific Mut. Life Ins. Co., 10 Cal. 2d 307 [74 P. 2d 761]; Neblett v. Carpenter, 305 U. S. 297 [59 S. Ct. 170, 83 L. Ed 182].)

In 1946, upon request of the requisite number of life policyholders, a price determination committee was appointed, and thereafter such committee determined that mutualization was practicable of accomplishment, promulgated a Plan of Mutualization, and fixed the price and terms of payment at which the life policyholders of New Company should have the right to acquire the stock of New Company from the liquidator (who had by that time become successor of the conservator) of Old Company.

On September 22, 1950, the Insurance Commissioner, after a lengthy hearing, found that the Plan of Mutualization was fair and equitable to the stockholder, as well as to all other interested parties, and approved the plan.

In response to the petition for a writ of mandamus filed by appellants for the purpose of inquiring into the validity of the Insurance Commissioner's approval of the Plan of Mutualization there were presented to the Superior Court the questions of whether the Insurance Commissioner proceeded without or in excess of his jurisdiction, and whether the commissioner accorded a fair trial to those opposing the plan, and whether the commissioner committed any prejudicial abuse of discretion, particularly whether the commissioner proceeded in the manner required by law, and whether his approval of the plan was supported by substantial evidence in the light of the whole record. After a hearing, the judge of said court filed a carefully prepared opinion, in which he held that the Insurance Commissioner had not acted without or in excess of his juridiction, had accorded a fair trial to those opposing the plan, and had not abused his discretion in approving the plan.

Since appellants raise questions as to whether the rehabilitation and reinsurance agreement dated December 4, 1936, is valid in respect of the option to mutualize granted to the participating life policyholders; whether the validity of such agreement is *res judicata;* whether New Company, which has been carrying on a nationwide insurance business since 1936, should now be treated as insolvent for the purposes of mutualization; whether the requisite statutory steps were taken for mutualization of New Company, and whether the price determination committee acted in good faith in fixing the price and terms of payment for the stock of New Company, it is essential to present in some detail what preceded the Insurance Commissioner's hearing as well as what took place at the hearing.

Old Company was engaged in the business of writing both participating and nonparticipating life insurance and accident and health insurance. The report of the regular Triennial Convention examination of Old Company made as of December 31, 1935, showed that Old Company was insolvent. The insolvency arose out of the fact that the premium rates charged by Old Company to the holders of

noncancellable accident and health policies (hereinafter referred to as "non-can policies") were inadequate. The result was that the reserves for non-can policies were inadequate and Old Company was insolvent by at least $17,000,000. Said report was filed with the Insurance Commissioner on July 21, 1936. On July 22, 1936, pursuant to the provisions of Section 1011 of the Insurance Code, the Insurance Commissioner filed with the Superior Court in Los Angeles an application for an order appointing him conservator of Old Company and vesting in him title to all of the assets of that company. We shall hereafter refer to such proceedings as "conservatorship proceeding."

Said application was presented to Judge Douglas L. Edmonds, then presiding judge of said court, and Judge Edmonds on July 22, 1936, signed the order applied for. Pursuant to said order and pursuant to Section 1013 of the Insurance Code, which authorized seizure without notice or court order, the Insurance Commissioner took possession of all of the assets of Old Company. (Carpenter v. Pacific Mut. Life Ins. Co., *supra*, 10 Cal. 2d 307, 314-317.)

On July 22, 1936, Judge Edmonds also signed "Order Permitting, Approving and Authorizing Rehabilitation Sale and Transfer of Assets and Reinsurance Plan and Agreement of The Pacific Mutual Life Insurance Company of California" pursuant to the provisions of Section 1043 of the Insurance Code. Said order, among other things, authorized the organization of New Company with a capital and surplus of $3,000,000, to be provided from the funds of the participating life division of the life department of Old Company. In addition thereto, the participating life division of the life department of Old Company was to furnish to New Company the sum of $1,792,-118.97 as a reserve for the non-can policies which were to be partially assumed by New Company under the rehabilitation agreement approved by Judge Edmonds. Said rehabilitation agreement further provided that the stock of New Company should be held by the Insurance Commis-

sioner as conservator, subject to the right of New Company to become mutualized "as soon as legally possible."

In accordance with Judge Edmond's order, the Insurance Commissioner organized New Company and the participating life policyholders contributed to New Company the total sum of $4,792,118.97, $3,000,000 of which constituted the capital and surplus of New Company, and $1,792,118.97 of which constituted a reserve for non-can policies which were to be partially assumed by New Company.

Said sum contributed by the participating life policyholders constituted all but $423,136.26 of the surplus of the participating life division of the life department of Old Company. Said sum had been earmarked for and was owned by the participating life policyholders of Old Company, because Old Company had conducted its participating life division as if it were a separate mutual life insurance company. A separate set of books had been maintained for the participating life division; specific expenses had been charged to said division, separate surplus had been maintained for said division; separate annual statements had been prepared for said division, and the so-called "dividends" or returns of premium made to participating life policyholders had been charged against the funds of said division.

After the organization of New Company the commissioner, as conservator, in accordance with Judge Edmonds' order, transferred to New Company substantially all of the assets of Old Company. As consideration for such assets, New Company delivered to the conservator all of the capital stock of New Company, which he was to hold, subject to the provisions of the rehabilitation agreement approved by Judge Edmonds. On July 23, 1936, New Company intervened and became a party to the conservatorship proceedings. Shortly thereafter it was found that Justice Edmonds was the owner of a policy of life insurance issued by Old Company, and that he was, therefore, disqualified. It was ultimately held that his orders were void (Carpenter v. Pacific Mut. Life Ins. Co., *supra,* 10 Cal. 2d 307, 323).

Upon discovery of Judge Edmonds' disqualification, the application of the Insurance Commissioner for appointment as conservator of Old Company was assigned to and heard by Judge Henry M. Willis, and on August 11, 1936, Judge Willis made a new order appointing the Insurance Commissioner as conservator and ratifying an appointment theretofore made by Judge Edmonds. It was held that notwithstanding the invalidity of Judge Edmonds' orders, the conservator's seizure of the assets of Old Company was lawful (Carpenter v. Pacific Mut. Life Ins. Co., *supra*, 10 Cal. 2d 324). However, Judge Willis did not, on August 11, 1936, make any order with respect to the rehabilitation agreement theretofore approved by Judge Edmonds or with respect to the transfer of Old Company's assets to New Company and the issuance of New Company's stock to the conservator. Nevertheless, New Company held the assets of Old Company and the conservator held all of the capital stock of New Company. In view of the fact that the rehabilitation of the business of an insolvent insurer and the transfer of assets of such an insurer can be made only with court approval (Ins. Code §§1043 and 1037 subd. d), the invalidity of Judge Edmonds' orders left the permanent status of the assets and the stock in suspense until Judge Willis's order of December 4, 1936, which will hereinafter be referred to.

During the period between July 22, 1936, and December 4, 1936, New Company acted as a corporate agent of the Insurance Commissioner to assist him in carrying on the business of the Old Company.

As was stated by the Supreme Court in the Carpenter case, *supra*: It was obvious that if the agency organization were to be preserved pending court approval of the rehabilitation plan, the business of the Old Company had to be continued. Faced with these facts, the commissioner determined to organize a New Company to continue the business pending the approval of a rehabilitation plan. And it was pending the approval of a rehabilitation plan that New Company acted as a corporate agent of the Insurance Commissioner. (Carpenter v. Pacific Mut. Life Ins. Co., *supra*, 10 Cal. 2d 307, 325.)

On August 29, 1936, Judge Willis ordered all interested parties to show cause why they should not approve the rehabilitation agreement which Judge Edmonds had theretofore purported to approve. Numerous parties, including individual stockholders and the Pacific Mutual Stockholders Protective Committee, filed objections to such rehabilitation agreement. (Carpenter v. Pacific Mut. Life Ins. Co., *supra*, 10 Cal. 2d 319.)

On September 25, 1936, the Insurance Commissioner filed a "Petition for Approval of the Rehabilitation and Reinsurance Agreement," attached to which was the rehabilitation and reinsurance agreement which constitutes the basis of the rights of the conservator and his successors as owners of all of the stock of the company, and the basis of the rights of appellants herein, who claim an equitable interest in the stock of New Company, and the basis of the rights of the participating life policy holders under the option contained therein to cause New Company to be mutualized. Said petition prayed for an order ratifying, confirming and approving the acts of the commissioner as conservator and causing to be formed, forming and subscribing to and purchasing the capital stock of New Company, and ratifying, confirming and approving the transfer and conveyance therefore made of the assets of Old Company to New Company. Said petition further prayed that the rehabilitation and reinsurance agreement be approved and that the conservator be authorized and directed to execute said agreement and to carry out its provisions.

On the same date, the court issued an order requiring Old Company, New Company, and all persons interested or claiming to be interested, either as policyholders or stockholders of Old Company, or otherwise, to show cause why the court should not make orders in accordance with the conservator's petition.

After a protracted hearing pursuant to said order to show cause, in which Pacific Mutual Stockholders Protective Committee, numerous individual stockholders and others were heard, Judge Willis made his order of Decem-

ber 4, 1936, in which he ratified, confirmed and approved the acts of the conservator in organizing and subscribing to and acquiring the capital stock of New Company, and in transferring to New Company the sum of $3,000,000 out of the assets in his hands as a conservator, and ratifying, confirming and approving the transfer and conveyance theretofore made of the assets of Old Company to New Company.

Said order approved "each and all of the terms and conditions" of the rehabilitation and reinsurance agreement and authorized and directed the conservator to enter into said agreement, and authorized him "without further order of this court, fully and faithfully to perform, carry out, and discharge each and all of the obligations, terms, conditions, and covenants on his part required to be performed under the terms of said Rehabilitation and Reinsurance Agreement," and "forever barred and enjoined [all persons] from making hereafter any complaint in respect of the said Rehabilitation and Reinsurance Agreement, or any provision or provisions thereof, except as in said agreement specifically permitted or by appeal from this Order; the prosecution by any person, firm, or corporation of any proceeding or proceedings of whatever kind or nature, for the purpose of attacking this Order, or any conveyance or transfer made pursuant hereto, (other than as permitted by said Rehabilitation and Reinsurance Agreement or by appeal from this Order)."

The Rehabilitation and Reinsurance Agreement provided for the transfer to New Company of substantially all of the assets of Old Company and for the reinsurance and assumption by New Company, at the election of the respective policyholders, of all policies of insurance other than non-can policies, and on reduced rates of benefit, for reinsurance and assumption by New Company at the election of the policyholders of all non-can policies of insurance. It provided that New Company should establish a participating department, whose assets should be held and whose business should be carried on in the same manner as if it constituted a separate mutual life insurance company. It further provided that New Company should

establish a separate department for its Nonparticipating Life Insurance, and a separate department for its Accident and Health Insurance, and that any surplus existing in said departments might be used for general corporate purposes subject to limitations contained in Paragraph 14 of said agreement.

In Paragraph 14 it was provided that a special fund should be established from funds available for general corporate purposes for the purpose of completely restoring the non-can benefits which had been reinsured and assumed on reduced basis. It was further provided that there should be transferred to such fund such amounts as the board of directors should in its discretion determine to be not reasonably required for the reasonable, proper and profitable conduct of the operations of New Company as a going concern. It was further provided that at the time of any examination of New Company by the Insurance Commissioner, the commissioner might require the transfer of additional funds to such special fund, to the extent that such additional funds available for general corporate purposes were, in his opinion, available without interfering with the proper and profitable conduct of the business of New Company as a going concern.

These provisions with respect to restoration of non-can benefits were made "to the end that the benefits originally provided in said Non-Can Policies as written may eventually be fully paid, including eventual full payment of benefits becoming due prior to the time of such restoration, with interest on deferred restoration payments of such benefits at the rate of three and one-half per cent (3½%) per annum."

The Rehabilitation Agreement provided for the transfer to New Company from the participating division of the life department of Old Company of the sum of $3,000,000 as capital and surplus and of the sum of $1,792,118.97 as a reserve for the Accident and Health Department, and further provided for the transfer to New Company, for its general corporate purposes, of not to exceed 10 per cent of the net profits on participating policies rein-

sured pursuant to said agreement. Profits from participating policies thereafter written were not to be affected thereby and were to be held in the walled-off participating department of New Company.

Paragraph 20(a) of the Rehabilitation and Reinsurance Agreement created an *option* in favor of the participating life policyholders to cause the company to be mutualized under the conditions specified therein. Said right of the participating life policyholders was referred to in Paragraph 20 as "an option to mutualize." It was provided therein that after a period of approximately 10 years, 10 per cent of the participating life policyholders could request the creation of an appointing committee to exercise duties in respect of a mutualization of New Company for the benefits of the departments of New Company designated by such policyholders; that the appointing committee should designate a price determination committee; that the price determination committee should determine whether, in its opinion, mutualization of New Company was then practicable and that, if it determined that mutualization was then practicable it should determine the proper price to be paid for the stock of New Company upon such mutualization and appropriate terms of payment. Said agreement provided further, in order that said option might be an effective option, binding upon the stockholder of New Company and all others claiming through such stockholder, that the conservator, as sole stockholder, for himself and for any successors in ownership of said stock, agreed to consent and consented to such Plan of Mutualization as might be promulgated by the price determination committee and to dispose of such stock at the price and upon the terms of payment provided for in such Plan of Mutualization.

Various provisions of the Rehabilitation and Reinsurance Agreement show that the agreement contemplated that the price determination committee could promulgate a Plan of Mutualization and fix the price and terms of payment for the stock prior to the full restoration of non-can benefits; and that in such case payment for the stock would be postponed until after a restoration of non-

can benefits had been completed. Inherent in the fact that the agreement contemplated such postponement of payment, is a further fact that the agreement contemplated that the Plan of Mutualization should not obligate New Company unconditionally to make the postponed payment.

Appeals were taken from Judge Willis's order of December 4, 1936, adjudicating the validity of the Rehabilitation and Reinsurance Agreement and the Supreme Court of California and the Supreme Court of the United States affirmed the order. (Carpenter v. Pacific Mut. Life Ins. Co., *supra.*)

The result of Judge Willis's order of December 4, 1936, was that New Company acquired valid title to substantially all of the assets of Old Company and the conservator acquired valid title to all of the capital stock of New Company, subject, however, to an option to the participating life policyholders of New Company, through mutualization proceedings initiated after approximately 10 years, to cause New Company to acquire such stock at the price and upon the terms fixed by a duly appointed price determination committee, in the event that such committee should determine that in its opinion mutualization was practicable. The option required that the mutualization proceedings should be conducted in accordance with the laws of the State of California.

On February 2, 1937, the court, in the conservatorship proceedings, ordered the liquidation of Old Company and appointed the Insurance Commissioner to liquidate it. The validity of this order was upheld on appeal. (Carpenter v. Pacific Mut. Life Ins. Co., 13 Cal. 2d 306 [89 P. 2d 637].)

Thus, the liquidator succeeded the conservator, as the owner of the stock of New Company, subject to the option in favor of the participating policyholders to cause the company to be mutualized.

On April 4, 1938, the liquidator transferred title to the capital stock of the New Company to voting trustees. This was done pursuant to the provisions of section

DARK PAGE

1037(e) of the Insurance Code. The validity of this transfer under the voting trust was upheld upon appeal. (Caminetti v. Pacific Mutual L. Ins. Co., 22 Cal. 2d 344 [139 P. 2d 908].)

Under the provisions of the voting trust, the trustees were given full legal title to the stock in order that they might exercise the rights of stockholders in the control of the corporation, and they were expressly obligated to carry out all of the provisions of the Rehabilitation and Reinsurance Agreement, including the covenant of the conservator, for himself and his successors in the ownership of the stock, to consent to any Plan of Mutualization promulgated by a duly appointed price determination committee.

Thus, the voting trustees held the stock of New Company subject to the option to mutualize contained in the Rehabilitation and Reinsurance Agreement. The voting trust provided that it should terminate upon adoption of a Plan of Mutualization in accordance with the laws of the State of California.

In 1946, approximately 10 years after the organization of New Company, the requisite percentage of participating life policyholders requested the creation of an appointing committee to exercise the duties and functions provided for in the Rehabilitation and Reinsurance Agreement in respect of a proposed mutualization of New Company. The participating life policyholders, as permitted by the agreement, specified that the mutualization should be for the benefit of both participating and non-participating life policyholders. As of January 31, 1947, in accordance with the terms of said agreement, George Willard Smith, President of the Life Insurance Association of America (formerly the Association of Life Insurance Presidents), Doctor Donald B. Tresidder, President of Stanford University, and Doctor Clarence A. Dykstra, Provost of the University of California at Los Angeles, appointed a price determination committee consisting of Alva J. McAndless, Ray D. Murphy, Horace R. Bassford, and Albert J. Hettinger. Mr. McAndless was the President of Lincoln

National Life Insurance Company of Fort Wayne, Indiana, a stock company, and the tenth largest life insurance company in the United States. He was a graduate of the University of Michigan and an actuary by profession. He was a past president of the American Institute of Actuaries (now called the Society of Actuaries) and a past president of the American Life Convention. He had been connected with Lincoln National Life Insurance Company since 1919 and had risen through the ranks, holding various positions and offices until he became president in 1939. He had had extensive experience in evaluating other life insurance companies through the acquisition of stock companies, either by way of acquiring their stock or their assets. Among the acquisitions with which he was familiar or in which he personally participated were acquisitions which Lincoln National Life Insurance Company made of Michigan State Life Insurance Company, Pioneer Life Insurance Company, Merchants Life Insurance Company, Globe Life Insurance, American Life Insurance Company, Reinsurance Life Insurance Company, Old Line Life Insurance Company, Northern States Life Insurance Company, and Royal Union Life Insurance Company. In addition thereto, he had handled negotiations for the purchase of Illinois Life Insurance Company and Missouri State Life Insurance Company, but in those instances Lincoln National Life Insurance Company did not become the purchaser.

Mr. Murphy was the Vice President and Chief Actuary of the Equitable Life Assurance Society of the United States, one of the five largest life insurance companies in the country. He is a graduate of Harvard University and an actuary by profession. He had been with Equitable Life since 1913. He was a past president of the Actuarial Society of America. Since 1936 he had been responsible at Equitable Life for all valuations of life and accident and health contingencies, including noncancellable accident and health contracts. He was responsible at Equitable Life for mortality and morbidity investigations and for analysis of all sources of profits and losses, and for distribution of surplus based upon such analyses. His duty

caused him to be involved in many studies and estimates of projected future profits and losses and the effect of future contingencies upon the operations of Equitable Life.

Mr. Bassford was Vice President and Chief Actuary of Metropolitan Life Insurance Company, the largest life insurance company in the United States. He was a graduate of Trinity College and had been associated with Metropolitan Life since 1915. He was a Vice President of the Actuarial Society of America. He had participated in the acquisition by Metropolitan Life of several life insurance companies, including Pittsburg Life and Trust Company, Niagara Life Insurance Company, and Golden Seal Association, in connection with which it was necessary for him to evaluate said companies.

Mr. Hettinger was a partner in the investment banking firm of Lazard Freres and Company. He was a graduate of Stanford University and received the degree of Doctor of Philosophy in Business Economics at Harvard University, where he served for a number of years as Professor of Business Economics in the Harvard Graduate School of Business Administration. As a member of the Harvard faculty he had supervised research work in the valuation of life insurance stocks, and during the same period acted as economist to the Governor of the Federal Reserve Bank of Boston. He became engaged in business in the investment field in 1926 and became a partner in Lazard Freres and Company in 1943. During his business life he had made a particular study of life insurance stocks and their values.

Following their appointment on January 31, 1947, the members of the price determination committee undertook to perform the duties and responsibilities entrusted to them. They employed as their actuary Joseph A. Christman, Associate Actuary of the Metropolitan Life Insurance Company of New York. He was a Fellow of the Actuarial Society of America and had served in the Actuarial Division of Metropolitan Life since 1926. In the performance of his duties for Metropolitan Life, approximately 600 employees worked under his supervision.

Associated with him in the duties which he performed for the price determination committee were D. J. van Keuren and F. H. Byron, both employees of the Metropolitan Life and Fellows of the Actuarial Society of America. Mr. Christman and his colleagues had the assistance of numerous trained supervisory and clerical employes borrowed from Metropolitan Life and Equitable Life.

Commencing in 1947, the members of the price determination committee, with the assistance of Mr. Christman and his associates, undertook a study of the past and anticipated future earnings of New Company, of the amount which would be required completely to restore non-can benefits, of the length of time which would be required to accomplish such restoration, and of the value of the stock of that company. Their study occupied a period of approximately three years and consumed approximately 10,000 hours of work. Mr. McAndless testified that the committee made "one of the most complete investigations of earning power that has ever been made for any life insurance company."

On April 4, 1950, the price determination committee rendered its report, stating that in its opinion mutualization of New Company was then practicable, determined the value of the stock as of December 31, 1948, and fixed the price to be paid for the stock of New Company at $3,000,000 plus interest on $3,000,000, from December 31, 1948, to date of payment, with certain provisions for its augmentation, and fixed the terms of payment.

The Plan of Mutualization provides for a special surplus fund, to be accumulated from 5 per cent of the net profits of the participating department on policies issued subsequent to July 22, 1936, and for a payment of the purchase price from this fund and from capital in general corporate surplus. The Plan of Mutualization filed by the committee as part of its report, provided that upon adoption of the plan, the Voting Trust Agreement of April 4, 1938, should terminate in accordance with the provisions of said voting trust and that the liquidator to whom the voting trustees were obligated to transfer the

stock should immediately dispose of the stock of New Company by transferring it to trustees under a new voting trust, in accordance with the provisions of Insurance Code, Section 11529.5. It was expressly provided that nothing contained in the plan should affect the right of the non-can policyholders to have applied to restoration of non-can benefits all of the corporate earnings of the company not reasonably required for the reasonable, proper and profitable conduct of the operations of New Company as a going concern, as provided in Paragraph 14 of the Rehabilitation and Reinsurance Agreement.

The plan further provided that in accordance with such agreement New Company should submit the plan to the policyholders entitled to vote thereon and that if 10 per cent of such policyholders should so request New Company should submit the plan for approval in accordance with the laws of the State of California.

The plan was submitted to the life policyholders and the requisite percentage requested its submission for approval in accordance with the laws of the State of California. In accordance with Section 11526 of the Insurance Code, New Company submitted the plan for the required approvals; on May 5, 1950, the board of directors of New Company adopted the Plan of Mutualization. Thereafter, a majority of the voting trustees under the Voting Trust Agreement of April 4, 1938, as owners and holders of the stock of New Company, and in accordance with the provisions of said Voting Trust Agreement, approved the Plan of Mutualization by executing their written consent thereto. Under the provisions of the Voting Trust Agreement the action of a majority of the trustees constituted action of all of the trustees.

On or about June 16, 1950, New Company submitted the Plan of Mutualization to the Insurance Commissioner and petitioned for the approval thereof. The Insurance Commissioner gave notice by publication and by mail that a hearing would be held on August 1, 1950, for the purpose of determining whether the Insurance Commissioner should approve the plan. Notice of the hearing was mailed, among

others, to Old Company and to the Pacific Mutual Stockholders Protective Committee. On August 1, 1950, the hearing commenced, and continued from day to day until and including August 18, 1950. All persons desiring to be heard were heard, including the Pacific Mutual Stockholders Protective Committee. Old Company did not avail itself of the opportunity to be heard. Evidence both oral and documentary was received, and was incorporated in a reporter's transcript of over 500 pages.

On September 22, 1950, the Insurance Commissioner issued a 22-page decision, in which he found that the Plan of Mutualization protected the rights and interests of New Company, its policyholders and its shareholders, and that the plan would be fair and equitable in its operation, and in which he issued his approval, thus permitting the plan to become effective if it should be approved by a majority vote of the life policyholders and should thereafter be filed in the office of the Insurance Commissioner. (Ins. Code, §11526.)

The life policyholders of New Company thereafter approved the Plan of Mutualization in accordance with Section 11526(d) of said Code.

On or about November 9, 1950, before the plan was filed in the office of the Insurance Commissioner, after having been adopted by a vote of the directors of New Company, and after having been approved by the written consent of the shareholders of New Company and by the Insurance Commissioner (but before its approval by the life policyholders of New Company) appellants filed their petition for writ of mandamus and obtained an order staying the operation of the Insurance Commissioner's approval of September 22, 1950, expressly permitting, however, a vote of the life policyholders in accordance with Section 11526(d) of the Insurance Code.

In accordance with the provisions of the Code of Civil Procedure, Section 1094.5, a hearing was held by the court below. All of the record of the proceedings before the Insurance Commissioner was filed with the court. Appellants, respondent Insurance Commissioner, and respondent

New Company each filed lengthy briefs and lengthy arguments were made, which are reported in the Reporter's Transcript on Appeal. No evidence was received other than stipulations and the record before the Insurance Commissioner, consisting of the Reporter's Daily Transcript, the exhibits and the Insurance Commissioner's decision. On March 24, 1952, the judge of the court filed his memorandum of decision, and on June 2, 1952, he filed his findings of fact, conclusions of law and judgment, which are the subject matter of the appeal herein.

We will now proceed to a consideration of the law of the case. As above indicated, the principal points raised by appellants are two:

(1) The order made by the Insurance Commissioner was not justified by the evidence; and

(2) The order was made without jurisdiction.

We think neither claim is tenable and that the judgment of the lower court must be affirmed.

Point (1) may be rather quickly disposed of. After notice to all interested parties, a hearing, which took 13 days to complete, was had by the commissioner. Much evidence, both oral and documentary, was received by him. It is manifestly impossible to here set it forth at length. Suffice it to say we have examined it in detail, all of the volumes of the daily transcript of the evidence and the exhibits introduced, and we are not prepared to say that such evidence then taken and received was insufficient to justify the commissioner's ultimate conclusion that the plan was fair and equitable to, and protected the rights and interests of, all interested parties, including the stockholder, in whose right the appellants sue.

On the contrary, much of the evidence was based upon thousands of hours of study and investigation by persons who appear to have been well qualified experts, and we are well satisfied the commissioner acted upon adequate evidence. Two members of the Price Determination Committee and one of the actuaries employed by the Price Determination Committee testified at length as to the manner in

which, and the basis upon which, the committee arrived at the price to be paid by New Company for its stock when it consummated the proposed Plan of Mutualization. In substance they testified that they had, by long and exhaustive actuarial studies, determined the amount necessary to fully but gradually restore the benefits of the non-can policyholders; that they had then discounted these amounts at 3 per cent interest to their present value, and found that the present value of the amounts necessary for restoration was $22,000,000; that by similar studies they had established the probable earnings of New Company for each year, commencing with the year 1949 and extending to the year 2000; that by discounting the earnings for the years 1949 to 1974, both inclusive, at 3 per cent (only a portion of the earnings for the last year were so discounted), they determined that the company would be able to complete restoration of non-can benefits in the year 1974; that after the completion of restoration the stockholders of Old Company would be entitled to its earnings, and that the present value of these earnings from 1974 to perpetuity, discounted at 10 per cent, was $2,614,000; that by reason of the terms of the rehabilitation agreement it was necessary to add $500,000 to this amount, but that if certain risk elements had been disregarded, they thought it proper to deduct the sum of approximately $100,000, giving a present value to the stock of $3,000,000; that the calculated earnings upon which their estimate of the time within which to complete restoration of non-can benefits could be made, and upon which they base the present value of future earnings, were net earnings, after provision for contingency reserves.

They also testified that in their opinion a buyer could be found who would be willing to presently pay $3,000,000 for the stock of New Company and await the right to participate in the earnings of New Company for 25 years; that the stock of large life insurance companies currently had sold at 4.3 to 7.8 times of their estimated earnings after the deduction of voluntary reserves; that if the estimated earnings of New Company from 1948 to perpetuity were discounted to their present value at 10 per cent, that value

DARK P

would be less than the amounts necessary for full restoration, and there would be nothing left for the stockholders; that if the present value of the stock were fixed by giving a value to the nonparticipating life insurance in force at $20 per thousand, the value of the stock would be less than the amount necessary for restoration, and that, in their considered opinion, the price of $3,000,000 was a fair one to be paid to the stockholders.

They also testified that because the payment of the present value of the stock as determined by them was not to be made immediately, but was to be deferred, they had provided for the payment of interest upon the $3,000,000 and instead of fixing a rate of interest had used the basis of the highest coupon rate paid on long term government bonds, as they thought that would be equal to the amount New Company could earn upon the deferred payment from year to year; that they recognized that if restoration was completed sooner than they estimated, that is, prior to 1974, this would give an added value to the stock and that they believed $250,000 for each year by which the date of restoration preceded 1974, was a fair estimate of the increased value.

There was introduced into evidence the report of the actuaries who had made the studies upon which the cost of restoration of future earnings were based, and in which the method and the data used are set forth in detail; and much other direct and pertinent evidence.

Some point is made of the fact that some evidence available was not spread upon the record. In view of the foregoing, such is of no consequence. And, in any event, there is nothing in Section 1094.5, Code of Civil Procedure, or any other law we know of in proceedings such as this, which requires the spreading of detailed facts upon the record. (Popcorn Equipment Co. v. Page, 92 Cal. App. 2d 448, 451 [207 P. 2d 647)] *In re* Atlas Pipeline Corp., 39 F. Supp. 846, 848.) All that is required is that the commissioner's approval be supported by substantial evidence in the light of the whole record, and if such be the case, as we now hold it was, the court below and this court are bound thereby. (Thompson v. City of Long Beach, 41 Cal. 2d 235, 239-240

GE BLEED THRU

[259 P. 2d 649]; Rible v. Hughes, 24 Cal. 2d 437, 445 [150 P. 2d 455, 154 A. L. R. 137]; Housman v. Board of Medical Examiners, 84 Cal. App. 2d 308, 315 [190 P. 2d 653]; Republic Aviation Corp. v. National Labor Relations Board, 324 U. S. 793, 800 [65 S. Ct. 982, 89 L. Ed. 1372, 1377, 157 A. L. R. 1081].)

Point (2). We shall now proceed to a consideration of the question of jurisdiction and related matters. We think it proper to first consider the issue of *res judicata*. In this respect the appellants contend that the order of December 4, 1936, approving the Rehabilitation and Reinsurance Agreement is not *res judicata* as to such agreement, nor is it *res judicata* as to the Plan of Mutualization.

As to the first contention, we are foreclosed from considering it for the Supreme Court has already decided the point contrary to appellants' claim. In Carpenter v. Pacific Mut. Life Ins. Co., 13 Cal. 2d 306, 309 [89 P. 2d 637], the court said: "The legality of the seizure and the lawfulness and propriety of the plan of rehabilitation have already been upheld by this court. (Carpenter v. Pacific Mut. Life Ins. Co., 10 Cal. 2d 307 . . . affirmed with opinion, Neblett v. Carpenter, 305 U. S. 297 [. . . . 83 L. Ed. 182].)"

The California courts have quite uniformly held that when the validity of an agreement is adjudged in a prior proceeding, that issue is *res judicata*, even though a litigant in a later proceeding may urge some reason for its alleged invalidity which was not urged in the prior proceeding. (Price v. Sixth District Agricultural Assn., 201 Cal. 502, 509 [258 P. 387]; De Hart v. Allen, 26 Cal. 2d 829, 831 [161 P. 2d 453].)

In proceedings in which attacks have been made upon the validity of similar plans of rehabilitation after an adjudication of the validity of such plans, the courts have held the issue of validity to be *res judicata* as to all parties represented in the proceedings for the approval of such rehabilitation plan, as to persons in privity with such parties, and as to parties represented by them through class representation. (Thrower v. Kistler, 14 F. Supp. 217, 219,

221; National Surety Corp. v. Nantz, 262 Ky. 413 [90 S. W. 2d 385, 388].)

The fact that a series of orders were contemplated does not change the rule. One of a series of orders in a proceeding becomes *res judicata* if the order is appealable and not appealed from or if an appeal is taken and is affirmed on appeal. (Estate of Nolan, 145 Cal. 559, 561 [79 P. 428]; Baldwin v. Stewart, 218 Cal. 364, 367-368 [23 P. 2d 283].)

The issue of the Rehabilitation and Reinsurance Agreement was fully litigated in an adversary proceeding, and not by default. We have examined the authorities cited by appellants in support of their contention in this regard and find that they are not, in our opinion, authority for that which we are now investigating.

Appellants urge that before approving the Plan of Mutualization as fair and equitable the Insurance Commissioner was in duty bound to determine the value of the New Company as a going concern by ascertaining its earning capacity and capitalizing the same at an appropriate rate on the basis of economic surveys and special studies of the relevant criteria. In this case it was not necessary, as a matter of law, to employ any one method of determining the value of the stock. Such stock could be evaluated either on the basis of the market value, capitalization (so-called going concern and investment value), or on the basis of the usual method of evaluating all the stock of an insurance company. (California Annual Conf. of M. E. Church v. Seitz, 74 Cal. 287, 296 [15 P. 839]; Rives-Strong Bldg., Inc. v. Bank of America, 50 Cal. App. 2d 810, 816 [123 P. 2d 942]; Bewick v. Mecham, 26 Cal. 2d 92, 94-98 [156 P. 2d 757, 157 A. L. R. 1277].) At any rate, the Price Determination Committee did determine the investment value (or going concern value) of the stock, on the basis of a capitalization of corporate earnings applicable to the stockholders' equity.

In estimating future earnings there appears to be no specific criteria to go by. As the United States Supreme Court has said: "The extent and method of inquiry neces-

sary for a valuation based on earning capacity are necessarily dependent on the facts of each case." (Consolidated Rock Products Co. v. Du Bois, 312 U. S. 510, 527 [61 S. Ct. 675, 85 L. Ed. 982, 994].) The pattern of future earnings of the New Company having been fixed by the committee, upon sufficient evidence, we can see no objection to the plan adopted for capitalization. (Akron, Canton & Youngstown Ry. Co. v. Hagenbuch, 128 F. 2d 932, 939.)

The next point urged is that the Insurance Commissioner made no pretense of determining investment value in the manner required by law or otherwise; his order approving a Plan of Mutualization, therefore, was due to a mistake of law and must be reversed as arbitrary and constructively fraudulent. One answer to this is that the power and duty to determine the value and price of the stock was lodged in the Price Determination Committee and not in the Insurance Commissioner, by the Rehabilitation and Reinsurance Agreement, and this committee was thereby empowered to determine the price to be paid for the stock on any reasonable basis. The determination of value was made by the committee after considering several conventional and approved methods, and we are unable to hold, from the record, that the conclusion it arrived at was unreasonable.

Appellants complain that $3,000,000 was arbitrarily taken away from the stockholders by adding $3,000,000 to the estimated cost of restoration. We find this item to be fully explained in the Christman Report and in his testimony and we can find nothing arbitrary in his calculations. It is based on detailed study by actuaries.

In answer to appellants' contention to the contrary, we find it could well have been found, upon the evidence, that the Mutualization Plan did adequately protect the rights and interests of shareholders.

Appellants next contend that by approving Paragraph 20(f) of the Rehabilitation and Reinsurance Agreement, the court thereby reserved the jurisdiction to determine, at a future time, whether the provisions as to mutualization in Paragraph 20 were contrary to law or illegal or void.

We can see no merit in the contention. If the court had intended to reserve such power it would have said so. There is nothing in the order to that effect, and we should not and cannot read something into it that is not there. It is further urged that Paragraph 16 of Judge Willis's order of December 4, 1936, shows that the order is not *res judicata* as to the Rehabilitation and Reinsurance Agreement. The fact that the court therein reserved jurisdiction to make further orders in the premises, does not stultify, or set at naught, the order already made. This paragraph was obviously intended to permit the court to thereafter make whatever order it deemed proper, if any, to carry the order then being made along to fruition. (Cason v. Glass Bottle Blowers Assn., 37 Cal. 2d 134 [231 P. 2d 6].)

Passing now to the next contention of appellants, that the order of December 4, 1936, is not *res judicata* as to the Mutualization Plan proposed, we must, of course, agree, since the court could not then approve a plan which was not before it, nor, indeed, had it then been formulated; but what it did do was to approve the agreement in all of its details, and one of those details was to give the participating life policyholders the *right or option* to mutualize thereafter. The decreeing of this *right* is, therefore, *res judicata*. We are satisfied that the order we have been discussing has become *res judicata* as to all the matters determined therein.

We now pass to another point urged by appellants, and that is that sections 1043-1052 of the Insurance Code, and not sections 11526-11533, are applicable to the mutualization of the New Company.

In the first place, the rehabilitation agreement above referred to unquestionably makes sections 11525, etc., applicable to the mutualization of the New Company, and this agreement has been approved by the court, thus becoming *res judicata*. In the second place, these sections (11526-11533) would have been applicable in any event, because the New Company is a solvent insurer and not one that has been seized by the commissioner. Paragraph 20(a) of the agreement approved by the court, provides

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machinery for the formation of a "voluntary mutualization of the New Company, in accordance with the laws of the State of California." Under such law a voluntary mutualization can be accomplished only under the provisions of section 11525, etc., of the Insurance Code and not under the provisions of section 1043, etc., thereof. This being the case, it would seem unnecessary to consider the other points raised by counsel in this regard, since to do so would merely be reconsidering something that has already been decided by the Supreme Court.

The contention is made that the court must disregard the corporate entity of the New Company and treat it as though it were the Old Company. This matter has already been decided contrary to such claim. (Garrison v. Pacific Mut. Life Ins. Co., 83 Cal. App. 2d 1, 9 [187 P. 2d 893].)

There is nothing in the Carpenter case, 10 Cal. 2d 307, *supra,* indicative of a thought that the two companies were one and the same, at least after December 4, 1936. The entity of a corporation cannot be disregarded unless it be alleged and proved that the organization thereof was fraudulent or prompted by dishonesty and that injustice would be done if the corporate entity were not disregarded, and that there has been a cessation of the individuality and separateness of the corporation and the owners of its stock. (Judelson v. American Metal Bearing Co., 89 Cal. App. 2d 256, 262-263 [200 P. 2d 836], and cases therein cited.) Nothing of such a nature herein appears. The New Company was not an agency of the Insurance Commissioner subsequent to December 4, 1936, but even if it was, obviously such would not make the New Company the same as the Old Company.

Next we consider the claim of appellants that the directors of the New Company had no knowledge of the data on which the Plan of Mutualization was based, and in purporting to adopt the plan, acted as rubber stamps. Section 11525 of the Insurance Code provides that a Plan for Mutualization of a solvent insurance company may be carried out "by complying with the requirements of this chapter." One requirement is that the plan shall be

"adopted by a vote of a majority of the directors." It is conceded that this was done on May 5, 1950. No authority is cited for the proposition that directors' action, once taken, can be attacked on the ground of insufficient information, and there probably is none, for obvious reasons. In fact, the law is, no doubt, to the contrary. (6 Fletcher, Cyclopedia of Corporations, p. 296.) Furthermore, there is no merit in the statement that the directors were not adequately informed. Prior to April 13, 1950, each director had received a copy of the report of the Price Determination Committee and of the Plan of Mutualization. Furthermore, at its meeting on May 5, the Board received reports, heard the testimony of informed witnesses, all to the effect that the plan could be practically accomplished, having due regard to the interests of all persons interested in the New Company, that it was based on sound principles, was fair, just, equitable, financially feasible, and that the price to be paid and the terms of payment were reasonable and fair; all of which seems to be a complete answer to this point raised by appellants.

We now take up the claim that no valid approval of the Plan of Mutualization has ever been given on behalf of the stockholders, the consent purportedly given by the conservator in the Rehabilitation Agreement did not constitute a valid approval of the present Plan of Mutualization, and the liquidator or conservator could not delegate his power to the Price Determination Committee. The facts of this case take it out of the general rules of law enunciated in the authorities cited by appellants. Here, the validity of the rehabilitation agreement, wherein the conservator, for himself and his successors in interest, as shareholder of the New Company, consented and agreed to consent to such Plan of Mutualization as might be promulgated by a duly appointed Price Determination Committee, is, as is all other parts of said agreements, *res judicata*.

Thus, the proposition is not where a trustee, having certain duties to perform, on his own initiative delegates his authority or duties to another; rather is it a case where he is bound, both by contract and decree, to consent to

what another may do. He could not have refused to give his consent, had he wanted to, under the facts in this case.

We in no way intend to detract from the force of the foregoing conclusion in adding that agreements in which obligations depend on fact determinations thereafter to be made by third persons are valid and not unusual. There are many cases so holding. Illustrative thereof are: Bewick v. Meacham, 26 Cal. 2d 92, 97 [156 P. 2d 757, 157 A. L. R. 1277]; American-Hawaiian Engineering & Const. Co. v. Butler, 165 Cal. 497, 513 [133 P. 280, Ann. Cas. 1916C 44]; Roberts v. Security T. & S. Bank, 196 Cal. 557, 568 [238 P. 673]; Silva v. Mercier, 33 Cal. 2d 704, 708-709 [204 P. 2d 609]; Market Street Ry. Co. v. Hellman, 109 Cal. 571 [42 P. 225]; 3 Williston on Contracts, page 2247, section 800.

Another contention of the appellants is that the conservator or liquidator could not give his approval as trustee for the shareholders until after the adoption of the Plan of Mutualization by a vote of a majority of the board of directors, they specifically saying that the steps required to mutualize a solvent or delinquent corporation must be taken in the order enumerated in section 11526. We cannot agree. The section could easily have so provided, but it does not, except in subdivision (e) thereof, and we are not permitted to judicially legislate.

Also, if there could be any question about it, the fact that the language appearing in subdivision (e) is not made to apply to subdivisions (a), (b), (c), (d) is strongly persuasive that the Legislature did not intend that such provisions should apply to these other subdivisions. (Market Street Ry. Co. v. Hellman, 109 Cal. 571, 587 [42 P. 225]; Estate of Bull, 153 Cal. 715, 717 [96 P. 366]; In re Sekuguchi, 123 Cal. App. 537, 538 [11 P. 2d 655]; 23 Cal. Jur. 762.) At any rate, if the liquidator was the stockholder whose consent was required, his consent will be deemed to have been given at the proper time, because being bound by the conservator's agreement to consent, equity will regard that as done which should have been done. (Civ. Code, § 3529; Poultry Producers of Central

Calif. v. Nilsson, 197 Cal. 245, 254 [239 P. 1086].) It is wholly proper that substance should prevail over mere form.

Appellants complain that the Insurance Commissioner, prior to approving the Plan of Mutualization, did not conduct the type of hearing required by section 11527 of the Insurance Code. This is based principally upon the claim that the Insurance Commissioner did not have, or receive, proper evidence to justify his conclusion which approved the Mutualization Plan. The basic problem for the commissioner to determine was whether or not the price and terms of payment for the New Company stock were fixed in accordance with the rehabilitation agreement, for if they were, the Plan of Mutualization is fair and equitable because it gives the stockholder the price and terms he agreed to take.

The point is made that some of the witnesses who testified before the commissioner were interested witnesses. Such claim could go only to the weight of the evidence and not its admissibility. It does not appear here, in any event, that any evidence received by him was not trustworthy, nor that any committeeman or valuer or any witness was guilty of partiality, bad faith, or misconduct in their appraisals or testimony. Therefore, the point cannot be upheld. (Cecil v. Bank of America, 107 Cal. App. 2d 38 [236 P. 2d 408]; Riccomini v. Pierucci, 54 Cal. App. 606, 608 [202 P. 344].)

Another point raised by the appellants is that they have been deprived of substantive due process because the stock of the New Company was valued as of the present, that the time of payment was fixed long in the future, payment was conditional, there was no provision for reasonable interest, and the price paid was grossly inadequate. On this question of due process we should never lose sight of the fact that the commissioner's approval of the Plan of Mutualization did not have the effect of taking appellants' property, since it was nothing more or less than a permit and did not compel the life policyholders to approve the plan, nor the stockholder to dispose of the stock as therein

provided, or the New Company to adopt the plan. Even after the commissioner's approval the life policyholders could have rejected the plan, had they so desired. The stockholder could have rejected the plan but for the Rehabilitation and Reinsurance Agreement, which obligated the stockholder to dispose of the stock at the price and upon the terms fixed by the Price Determination Committee. The compulsion upon the stockholder flows from the obligations of the Rehabilitation and Reinsurance Agreement and not from the commissioner's approval of the plan. Even if this were not so, we do not believe the point raised is sound. As we read the evidence it does not necessarily lead to that conclusion; in fact, it could well lead to a contrary conclusion, the one that was adopted by the Insurance Commissioner and upheld by the lower court, to wit, that the plan was fair and equitable.

This already lengthy opinion must come to a conclusion. We have carefully read the briefs of all parties and each point raised by the appellants. Those not hereinabove discussed, we find to be without substantial merit.

The record shows that the commissioner's order approving the Mutualization Plan was not improper, on the evidence submitted. As above indicated, the liquidator was bound by the rehabilitation agreement to dispose of the stock of the New Company on the terms fixed by the committee. Petitioners were parties to the proceeding in which the rehabilitation agreement was proposed, and their representatives participated in seeking that approval. They may not now complain of its terms.

The evidence before the commissioner was fully documented with respect to all factual data, the witnesses who testified appear to be outstanding in their fields, and their expert judgment on questions of valuation and valuation methods, interest rates and trends, and all other matters within the province of expert opinion, could not be disregarded on the basis of "mere unsupported suggestions and opinions as counsel." In that situation the commissioner could clearly have come to the conclusion that the plan should be approved.

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We have studied this case diligently in an effort to ascertain if there was error committed in the court below. We can find none of any consequence.

The oral argument of this case was regularly set for hearing by this court for February 10, 1954. On February 1, 1954, the parties hereto signed, and on February 8, 1954, filed herein a stipulation waiving oral argument and agreeing that the case "may be submitted for decision upon the briefs and record on file." On February 10, 1954, appellants appeared before the court and made an *ex parte* application to have the court consider a purported agreement between Old Company and one Clint W. Murchison, wherein the latter agreed, subject to a number of highly important contingencies, to pay $17,000,000 for stock in Old Company.

Various briefs have been filed herein, mostly by *amici curiae*, respectively approving and opposing such application. We have concluded we may not give consideration to such agreement. (Redsted v. Weiss, 71 Cal. App. 2d 660, 666 [163 P. 2d 105]; Bassett v. Johnson, 94 Cal. App. 2d 807, 812 [211 P. 2d 939].)

If we were to give full consideration to the offer, as made, we would be in no position to hold that the Insurance Commissioner erred in his conclusions, since such evidence could, at the most, to be merely cumulative. (Katenkamp v. Union Realty Co., 36 Cal. App. 2d 602, 621-622 [98 P. 2d 239].)

And, in any event, such additional evidence obviously would not be "so conclusive that it compels the direction of a judgment in favor of appellant," nor would its effect upon this appeal be "decisive." (Bassett v. Johnson, *supra.*)

While the last 18 years' history of this company is no proof thereof, nevertheless, it is a well recognized principle that all litigation must sometime come to an end.

The judgment of the lower court must be, and is, affirmed.

Dooling, J., and Kaufman, J., concurred.

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APPENDIX C.

Opinion of the Superior Court

In the Superior Court of the State of California in and for the County of Los Angeles.

The Pacific Mutual Life Insurance Company of California, etc., et al., Petitioners, vs. Wallace K. Downey, etc., et al., Respondents. No. 579,832.

Filed March 24, 1952.

MEMORANDUM OF DECISION

By this proceeding petitioners seek to review and set aside the order of the Insurance Commissioner approving a plan of mutualization of Pacific Mutual Life Insurance Company (hereinafter called New Company).

The factual and historical background, so far as is necessary to understand the numerous questions raised by petitioners, is as follows:

In 1936 Pacific Mutual Life Insurance Company of California, hereinafter referred to as Old Company, became insolvent. In July of 1936 the Insurance Commissioner, in accordance with the provisions of Section 1011 of the Insurance Code, filed an application for an order appointing him Conservator of Old Company. Pursuant to this application an order was made appointing the Commissioner as Conservator of Old Company, and vesting in him title to all the assets of that Company.

At the same time the court made an order which, among other things, authorized the organization of New Company, a respondent herein. In accordance with the order, the Commissioner organized New Company and transferred to it substantially all of the assets of Old Company, and received all of the stock of New Company, subject to the provisions of a rehabilitation agreement, which had been approved by the order last above mentioned.

It was thereafter found that Judge Edmonds, who had signed the order heretofore mentioned, was a policyholder in Old Company and was, therefore, disqualified, and that the orders he had made were void.

Thereafter a new application was made for the appointment of the Insurance Commissioner as Conservator, and this was heard by Judge Willis, and granted. Thereafter, upon notice, Judge Willis approved a rehabilitation agreement between New Company and the Insurance Commissioner as Conservator of Old Company. This agreement is in evidence in the present proceeding as Exhibit 9-A, and is hereinafter referred to as "Rehab" or "Rehab agreement."

In substance, insofar as the provisions thereof are pertinent in the present proceeding, the agreement provides that the Conservator should convey and assign to New Company all of the assets of Old Company, with certain exceptions; that New Company would reinsure the liability of Old Company and the Conservator under all insurance contracts issued by Old Company, except policies known as "non-can policies," which were policies of disability insurance issued by Old Company under which it had no right of cancellation so long as premiums were paid by the insured; that New Company would reinsure and assume the liability of Old Company and of the Conservator on all non-can policies, but at reduced amounts, varying from 20 per cent of the amounts payable under the face of the policy to 90 per cent of the amounts so payable; that if the Commissioner was appointed Liquidator of Old Company, New Company would pay to him an amount equal to the claims filed with and established against the Liquidator by such policyholders of Old Company as did not elect to accept reinsurance in New Company.

By paragraph 14 of Rehab it was agreed that New Company should, from time to time, transfer, from the funds of New Company available for its general corporate purposes, to a special fund such amounts as New Company's board of directors should determine to be not reasonably required for the reasonable and proper conduct of the operation of New Company, and that the Commissioner, at the time of any examination of New Company by him, might require the transfer of additional funds to such special fund.

AGE BLEED THRU

It was further provided that the moneys and assets from time to time placed in said special fund should be used by New Company to restore to the holders of non-can policies entitled thereto, benefits in excess of the amounts which were reinsured by New Company, to the end that the benefits "originally provided in said non-can policies as written may eventually be fully paid . . . with interest on deferred restoration payments . . . at the rate of three and one-half per cent . . ."

By paragraph 19 of Rehab it is provided that the Conservator or Liquidator should proceed in such manner and at such time as he thought proper, "subject to the provisions of paragraph 20 hereof," to realize upon the assets held by him; that the proceeds realized from the sale of any assets, other than assets received for the benefit of policyholders of Old Company who had rejected reinsurance by New Company, should be used by the Liquidator for the payment of any of his costs and expenses of administration and claims having preference in liquidation.

As to the balance of the amounts so realized, the agreement provides in part as follows:

"(b) In the event benefits under Non-Can Policies shall not theretofore have been fully restored as provided in paragraph 14 hereof, a portion of the remaining proceeds (but not exceeding the amount required to provide complete restoration of the benefits under Non-Can Policies), in the ratio which exists between the Non-Can Policies (evaluated as provided in subparagraph (b) of paragraph 17 hereof) whose holders have accepted reinsurance hereunder, and all Non-Can Policies (evaluated as provided in subparagraph (b) of paragraph 17 hereof), whether their holders have accepted reinsurance, or have rejected reinsurance hereunder, and have filed claims in the liquidation proceedings shall be paid to the New Company, and by it transferred to the special fund described in paragraph 14 hereof . . .

"(c) Any portion of such proceeds remaining after making the payments described in subparagraphs (a) and (b)

DARK P

hereof shall be used to pay and discharge claims filed with the Liquidator and finally allowed.

"(d) Any portion of such proceeds remaining after making the payments described in subparagraphs (a), (b), and (c) hereof shall be paid to the New Company for the purpose of the special fund described in paragraph 14 hereof, to the extent the same may be required to provide full restoration of the benefits under Non-Can Policies.

"(e) Any portion of such proceeds remaining after making the payments described in subparagraphs (a), (b), (c), and (d) hereof shall be disposed of by the Liquidator in the manner provided by law."

Paragraph 20 of the agreement provides that neither the Conservator nor the Liquidator should dispose of any of the stock of New Company held by him, except in one of the manners provided for in said paragraph. It was then provided that at any time "between July 1, 1946, and January 1, 1948, and thereafter so long as the Conservator or a Liquidator of the Old Company may continue to hold any or all of said stock," 10 per cent of the holders of participating policies of life insurance might request New Company to create an appointing committee, which should consist of the holders of certain named designated offices, and that this appointing committee should then designate "a Price Determination Committee of not less than three and not more than five persons skilled in matters of insurance company valuation, which committee . . . shall determine whether in their opinion the proposed voluntary mutualization of the New Company . . . *can then be practicably accomplished, having due regard to the interests of all persons interested in the New Company.* If it be determined that such mutualization is not then practicable no further steps shall be taken in connection with a *possible mutualization* of the New Company under the provisions of this subparagraph until at least six months after the date of such determination."

It then provides that if in the opinion of the Price Determination Committee "mutualization is *then practicable,*" the Committee shall determine "the price to be paid upon

K PAGE BLEED THRU

such mutualization and appropriate terms of payment thereof," but that said determination should not be made prior to January 1, 1947.

The agreement then, after specifying certain items that should be taken into consideration by the Committee in determining the price to be paid, provides that the Committee shall, in its report to New Company, include a plan of mutualization of New Company, which plan should, in addition to any other relevant matters, specify "the price to be paid, the terms of payment, the persons by whom and the manner in which the right to vote the stock in New Company is to be exercised *pending complete* payment of the purchase price;" that the Committee "may provide in the plan for the creation of a voting trust . . . designate the initial voting trustees and make provision for the appointment of their successors. Unless the benefits under Non-Can Policies have theretofore been fully restored and claims against the Liquidator fully paid, such plan shall further provide that such mutualization shall not affect the provisions of paragraph *17* or of paragraph *14* hereof, or the right of holders of Non-Can policies to the restoration of benefits from the sources and in the manner therein provided."

The agreement then requires that New Company, upon the request of 10 per cent of its policyholders entitled to vote, shall submit the plan "in accordance with the laws of the State of California then in effect." It then proceeds: "The Conservator for himself and for any successors in the ownership of said stock claiming under him in any manner other than through a sale of said stock pursuant to the provisions of subparagraph (d) *hereof agrees to consent and hereby consents* as the holder and owner of the stock of the New Company to such plan of mutualization. In the event said mutualization plan *is adopted* . . . Liquidator . . . *shall dispose* of such stock in accordance with such plan."

The agreement then gives to the Price Determination Committee, if appointed prior to January 1, 1948, the power to extend the time "within which mutualization may be

DARK PA

effected hereunder for such period or periods of time as it may deem necessary for the orderly completion of mutualization proceedings as herein provided."

Subparagraph (b) of paragraph 20 provides a method of effecting a merger, consolidation, reorganization, or reinsurance of New Company, free from the effect of subparagraph (a) as to mutualization.

Subparagraph (c) gives Old Company the right, subject to the approval by the Court, to purchase from the Liquidator the shares of stock of New Company held by him, by paying to the Liquidator an amount sufficient to complete restoration of Non-Can benefits and the payment of all claims against and liabilities of the Liquidator, subject, however, to the rights of policyholders as to mutualization if such payment be made prior to January 1, 1948.

Subparagraph (f) provides as follows:

"(f) If the provisions of this paragraph 20, or of any one or more of the subparagraphs hereof, should be contrary to law or illegal or void, then such paragraph, subparagraph, or subparagraphs, shall be null and void, and shall be deemed separable from the remaining covenants and agreements in this agreement contained; and shall in no way affect the validity of any of the remaining provisions of this agreement."

In addition to approving the Rehab agreement and authorizing its execution by the Conservator, the order made by Judge Willis decreed that adequate provision is made by the Rehab agreement for each and every class of policyholder, creditor, and stockholder of Old Company, and "that neither said agreement nor the plan therein embodied" discriminated unfairly or illegally in favor of any policyholder, creditor, stockholder, or other person interested in Old Company, its property or assets, and that the "agreement and the plan therein embodied" and each did fairly and equitably protect and adjust the rights, obligations and liabilities of all persons concerned; that the Rehab agreement afforded "a feasible method of providing within a reasonable time full restoration of the benefits under the non-cancellable income policies" of Old Company.

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By the order the Conservator was authorized "without further order of this court" fully and faithfully to perform all of the obligations and terms and conditions and covenants on his part to be performed under the terms of Rehab agreement.

Paragraph 16 of the order provides:

"That this court, without relinquishing by these specific provisions any jurisdiction by it retained as a matter of law, do, and it does hereby, specifically retain and reserve jurisdiction of the within proceedings for the purpose of authorizing or approving any act of the Insurance Commissioner of the State of California done, or to be done pursuant to or in accordance with this order, and for the purpose of making or entering, upon application of the Insurance Commissioner of the State of California or of Pacific Mutual Life Insurance Company, any order, decree judgment, or ruling required, permitted, or requested to be done, made, or entered in connection with or pursuant to the terms of said agreement, or for the effectuation of the purposes thereof."

By paragraph 19 the Conservator and New Company were authorized to do all things necessary, desirable or proper to carry out the terms of Rehab or to effectuate its purposes.

From this order certain policyholders of Old Company appealed, and on the appeal the order was affirmed. (See *Carpenter v. Pacific Mutual Life Ins. Co.*, 10 Cal. 2d 307).

In 1937 an order was made directing the Insurance Commissioner to wind up and liquidate the business of Old Company and appointing him Liquidator. From this order an appeal was taken by certain policyholders, and on the appeal the order was affirmed. (See *Carpenter v. Pacific Mutual Life Ins. Co.*, 13 Cal. 2d 306.)

In 1938 the Liquidator transferred the stock of New Company to five voting trustees, pursuant to the provisions of Section 1037(e) of the Insurance Code enacted in 1937. Thereafter the Insurance Commissioner and certain

DARK PA

policyholders sought orders directing the New Company and the voting trustees to retransfer the stock to the Liquidator upon the grounds that the transfer to the voting trust was invalid. From the order denying these applications an appeal was taken, and on this appeal the order of the Superior Court denying the relief sought was affirmed. (*Caminetti v. Pacific Mutual Life Ins. Co.*, 22 Cal. 2d 344.)

Since 1936 all claims of policyholders who did not elect to accept reinsurance in New Company have been paid the principal amount of their claim without interest, but still claim interest against the Liquidator (their claim for interest as against New Company having been denied) to an amount of approximately $500,000. In said period New Company has restored to the holders of Non-Can policies which were reinsured by New Company 36 per cent of the amount by which the policies had been written down on reinsurance.

In 1946 New Company, in compliance with a request made by its policyholders, pursuant to paragraph 20 (a) of Rehab, created an appointing committee, and in January, 1947 the appointing committee created a Price Determination Committee composed of Horace R. Bosforth, Albert J. Hettinger, Jr., Ray D. Murphy, and Alva J. McAndless.

In April, 1950 the Price Determination Committee made its report to New Company. By this report they stated that they answered in the affirmative the question "whether in their opinion the proposed voluntary mutualization of New Company . . . can then be practicably accomplished, having due regard to the interest of all persons interested in the New Company," and attached as a part of their report a plan of mutualization of New Company.

Thereafter the Board of Directors of New Company passed a resolution adopting the plan submitted by the Price Determination Committee, and the voting trustees, without examination into or passing upon the merits of the plan or the sufficiency of the price to be paid by New Company for its stock, approved the plan. The plan was not,

E BLEED THRU

after its submission by the Price Determination Committee, approved by the Liquidator.

New Company submitted the plan to the Insurance Commissioner for approval, and after an extended hearing the Commissioner made his order approving the plan, and found that it protected the rights and interests of New Company, its policyholders and shareholders, and that it would be fair and equitable in its operation. It is this order which the petitioners, who are Old Company, and a committee of its stockholders, seek by this proceeding to review.

It may be noted here that none of the policyholders of New Company, nor any of the persons who hold claims against the Liquidator for interest, are parties to the proceedings in this court, or complain of the plan or the order of the Commissioner.

In substance, the plan submitted by the committee and approved by the Commissioner provides that the shares of New Company now held by the statutory voting trustees shall be immediately transferred to nine voting trustees, named in the plan (including the Insurance Commissioner), to be held by them subject to the terms and provisions set forth in the voting trust agreement, a form of which is annexed to and made a part of the plan; that the price to be paid by New Company for its shares is 3 million dollars, with simple interest at an annual rate equal to the highest coupon rate of United States Government bonds at the furthest maturity outstanding at the close of the preceding calendar year, plus $250,000 for each full calendar year by which the date of complete restoration of Non-Can benefits antedates December 31, 1973.

That this sum shall be paid by New Company at such time as, (a) the benefits to all Non-Can policies reinsured by New Company shall have been completely restored; (b) the funds standing in a special surplus fund to be created, plus the capital and surplus standing in general corporate accounts, equal or exceed the price of the shares, with interest as specified above; (c) that the financial condition

of the Company is such that, after paying for the shares, it shall have admitted assets in excess of its liabilities equal to the amount of four per cent of all of its admitted assets, plus 25 per cent of the premiums collected during the preceding calendar year on all group insurance written on a one-year term basis and all accident and health insurance.

That there is to be set aside in a special fund, to be used in part payment of the purchase price, 5 per cent of the net profits of the Participating Department of New Company.

That in the event the price of the shares shall not have been paid by December 31, 1983, the plan shall be considered to have failed, and the voting trust shall terminate, the shares be returned to the Liquidator, and the amount standing in the special fund shall revert to the general surplus of the Participating Department of New Company.

It will serve no useful purpose to set forth here a synopsis of all of the evidence received before the Commissioner, but it is necessary to state the substance of a portion of that evidence, in order that certain questions raised, and my ruling thereon, may be clear.

Two members of the Price Determination Committee and one of the actuaries employed by the Price Determination Committee testified at length as to the manner in which, and the basis upon which, the committee arrived at the price to be paid by New Company for its stock when it consummated the proposed plan of mutualization. In substance they testified that they had, by long and exhaustive actuarial studies, determined the amount necessary to fully but gradually restore the benefits of the Non-Can policyholders; that they had then discounted these amounts at 3 per cent interest to their present value, and found that the present value of the amounts necessary for restoration was 22 million dollars; that by similar studies they had established the probable earnings of New Company for each year, commencing with the year 1949 and extending to the year 2000; that by discounting the

earnings for the years 1949 to 1974 (both inclusive) at 3 per cent (only a portion of the earnings for the last year were so discounted), they determined that the Company would be able to complete restoration of Non-Can benefits in the year 1974; that after the completion of restoration the stockholders of Old Company would be entitled to its earnings, and that the present value of these earnings from 1974 to perpetuity, discounted at 10 per cent, was $2,614,000; that by reason of the terms of the rehabilitation agreement it was necessary to add $500,000 to this amount, but that as certain risk elements had been disregarded, they thought it proper to deduct the sum of approximately $100,000, giving a present value to the stock of 3 million dollars; that the calculated earnings upon which their estimate of the time within which to complete restoration of Non-Can benefits could be made, and upon which they based the present value of future earnings, were net earnings, after provision for contingency reserves.

They further testified that in their opinion a buyer could be found who would be willing to presently pay 3 million dollars for the stock of New Company and await the right to participate in the earnings of New Company for 25 years; that the stock of large life insurance companies currently sold at 4.3 to 7.8 times of their estimated earnings after the deduction of voluntary reserves; that if the estimated earnings of New Company from 1948 to perpetuity were discounted to their present value at 10 per cent, that value would be less than the amounts necessary for full restoration, and there would be nothing left for the stockholders; that if the present value of the stock were fixed by giving a value to the nonparticipating life insurance in force at 20 dollars per thousand, the value of the stock would be less than the amount necessary for restoration, and that, in their considered opinion, the price of 3 million dollars was a fair one to be paid to the stockholders.

They further testified that because the payment of the present value of the stock as determined by them was not to be made immediately, but was to be deferred, that they had provided for the payment of interest upon the 3 million

DARK P

dollars, and instead of fixing a rate of interest had used the basis of the highest coupon rate paid on long-term Government bonds, as they thought that would be equal to the amount New Company could earn upon the deferred payment from year to year; that they recognized that if restoration was completed sooner than they estimated, that is, prior to 1974, this would give an added value to the stock, and that they believed $250,000 for each year by which the date of restoration preceded 1974, was a fair estimate of the increased value.

There was introduced into evidence the report of the actuaries who had made the studies upon which the cost of restoration and future earnings were based, and in which the method and the data used are set forth in detail. (Exh. 28).

Petitioners attack the order of the Commissioner and the plan of mutualization from many angles, but before passing on points made by them, there are certain questions which, to a large extent, underlie most of the points raised by them, and which must first be disposed of.

At all times we must keep in mind the nature of this proceeding. I have heretofore ruled, and again rule, that in this proceeding the court is not entitled to exercise its independent judgment as to any issue of fact, but must affirm the order of the Commissioner and deny the peremptory writ of mandate sought by the petition, if the Commissioner had jurisdiction, if there was a full and fair hearing before him, held in the manner fixed by statute, and if, viewed in the light of the whole record, his order is supported by substantial evidence.

Petitioners contend that before the Commissioner would have jurisdiction to hold a hearing or to make any order, the plan of mutualization submitted to him must first have been adopted by the Board of Directors of New Company and consented to by the Liquidator as the beneficial owner of all of the shares of New Company.

Respondents contend that these are not essential to the jurisdiction of the Commissioner, and that the Commissioner may make an order approving of the plan before

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it is adopted by the Board of Directors of New Company, or before any assent to it is given by the shareholders.

Commissioner's power to act is purely statutory, and he did not have the power to make the order here under review unless the statute, Section 11526 of the Insurance Code, was substantially complied with. That section specifies four steps that must be taken in the adoption of a plan of mutualization. They are: (a) Adoption by a vote of the majority of the directors of the corporation to be mutualized; (b) Approval by a vote of the majority of the outstanding shares of the corporation, or the written consent of such shareholders; (c) Submission to and approval by the Commissioner; (d) Approval by a majority vote of all the policyholders of the class or classes for whose benefit the stock is to be acquired and who cast their vote; (e) Filing in the office of the Insurance Commissioner after steps (b), (c), and (d) have been taken.

I am of the opinion that the Legislature intended that the steps set forth should be taken in the order named, and this is the construction placed on the plan by the Commissioner and by respondents prior to the sufficiency of the consent by the shareholder having been raised in this proceeding. (As to the Commissioner's construction of the statute, see Transcript, Volume I, page 3.)

If any other construction is placed upon the section, it would serve no purpose. Until a plan is adopted by the corporation, there is nothing for the stockholders to vote upon. Until a majority of the stockholders have approved a plan submitted by the corporation, there is no plan which could be submitted to the Commissioner. If a plan were promulgated by the Company and then taken to the Commissioner and, after he had acted so as to approve the plan, the shareholders refuse to approve, the Commissioner's action would have been futile and useless, and it would be necessary for him again to pass on a plan to which a requisite number of shareholders had agreed. If the plan were first submitted to the policyholders and then to the Commissioner, and later either the directors or the shareholders refused to approve, again his action would have been useless.

Certainly this section contemplates that there must be some agreement between the parties who will be bound by the plan, if it be approved, before the Commissioner is called upon or authorized to approve or reject it. I hold, therefore, that unless under the facts shown by the record, the shareholder did approve the plan prior to its submission to the Commissioner, he was without jurisdiction to act thereon.

Petitioners contend that the order made by Judge Willis in the liquidation proceeding is not a final order, and is, therefore, not res judicata, but that that order and the Rehab agreement are both subject to collateral attack in this proceeding.

The point is not well taken. The proceeding in which the order was made (to which I have referred and will refer to as "liquidation proceeding") was one authorized and had under Section 1043 of the Insurance Code. It was not an ex parte proceeding, but an adversary one. It was upon notice, and Old Company, one of the petitioners herein, and certain of its stockholders, appeared.

In that proceeding, Conservator, by his petition, sought authorization from the court to execute the Rehab agreement and directly tendered the issue as to the validiy of that agreement, and each of its terms and conditions.

The order not only approved the agreement and authorized its execution by the Conservator, but directly adjudged its validity and fairness.

Every attack made by petitioners here upon the Rehab agreement and the order approving it could have been made in the liquidation proceeding.

The proceedings had under Section 1043 of the Insurance Code is the method provided by statute for securing an adjudication of the validity of a plan for rehabilitation. The order made approving such plan is a final, not an interlocutory order. Until the order is made the plan is not a binding agreement. When it is made, the plan becomes an effective agreement between the parties. An order approving the plan gives life to it. An order reject-

AGE BLEED THRU

ing a plan kills it. The proceedings and the order made were not preliminary. They were the final step taken by the Conservator in rehabilitating the business of Old Company.

I hold, therefore, that neither the validity of the plan nor of the order approving it may be attacked in this proceeding. In view of this, it is unnecessary to pass upon many questions raised by the parties here.

Petitioners contend that inasmuch as Rehab did not set up a plan of mutualization, the court by that order did not pass upon the question as to whether or not the present plan of mutualization approved by the Commissioner was feasible, reasonable, fair, or equitable.

It is quite true that the court in the liquidation proceeding did not act or pass upon any plan of mutualization. The court in the liquidation proceeding did not have, and has not now, jurisdiction of mutualization proceedings. That jurisdiction is vested in the Commissioner, subject to limited review in this proceeding. The court in the liquidation proceeding did have jurisdiction to pass upon the validity of the plan of rehabilitation set forth in the agreement before it, and the provisions of Section 20 of that agreement are an integral part of the plan that it approved and found valid.

Petitioners further contend that the court in the liquidation proceeding did not determine the validity of Section 20 because of the severability of clause (subparagraph (f) of that paragraph) which has been heretofore quoted. They assert that the provisions of subparagraph (f) of paragraph 20—that if any paragraph or subparagraph should be "contrary to law or illegal or void," then said paragraph or subparagraph should be deemed separable from the remaining covenants and in no wise affect the validity thereof—as the grant of a continuing right to any interested person to at any time attack the legality of paragraph 20 or any proceedings had thereunder. They assert that as the order of Judge Willis approved all of the terms and conditions of the rehabilitation agreement,

DARK P

it approved subparagraph (f) and therefore continued it in effect.

I think they misconstrued the purpose of subparagraph (f). The purpose thereof was undoubtedly to enable the court in the proceeding had for the approval of Rehab either to approve the plan as a whole, or if it believed certain portions of paragraph 20 to be illegal, then to approve it with those parts deleted. In other words, the petitioners there said to that court: "We ask you to approve this agreement as a whole, but if you cannot give your approval to it as a whole, we ask you to approve it, after deleting therefrom such portions of paragraph 20 as you find contrary to law."

They thus submitted to the court by their petition the validity of all of the terms and conditions of paragraph 20, and when the court gave its approval of the agreement, without finding any provision of paragraph 20 to be contrary to law, it, by its judgment, established the validity of each of the provisions of that paragraph, and it became an integral part of the approved agreement; subparagraph (f) had then served its purpose.

Petitioners next contend that by paragraph 16 of its order approving the rehabilitation agreement, the court reserved the right to pass upon any plan of mutualization which might be thereafter submitted pursuant to paragraph 20 of Rehab and upon the fairness of the price to be paid for the stock of New Company under such plan.

The court in the liquidation proceedings had no jurisdiction, and does not now have jurisdiction to pass upon any plan of mutualization. That jurisdiction is given by statute to the Commissioner of Insurance. The court in the liquidation proceeding, however, did have jurisdiction and was required to approve or withhold approval of any plan of rehabilitation, and it had jurisdiction to approve any transaction affecting assets in the hands of the Conservator or Liquidator. Its jurisdiction and its duties as to the rehabilitation agreement are fixed by Section 1043 of the Insurance Code. Its jurisdiction and its duty as to transactions involving assets in the hands of the Con-

GE BLEED THRU

servator are fixed by subdivision (d) of Section 1037 of the Insurance Code.

I think it is apparent that the court did not reserve jurisdiction to pass upon the feasibility, fairness, justness or equitableness of any future plan of mutualization presented in accordance with paragraph 20, or to pass upon the fairness of the price fixed by such agreement, but that it actually exercised its jurisdiction by approving Rehab agreement.

It must be remembered that inasmuch as the orders of Judge Edmonds were void, the Conservator's title to the stock of New Company was not vested until Rehab was approved and executed.

Paragraph 20 was an integral part of the rehabilitation agreement, and when that agreement was approved and the Commissioner executed it, he accepted title to the shares of New Company subject to the conditions set forth in paragraph 20, that is, to the right of New Company to acquire that stock through mutualization proceedings had in accordance with the provisions of that paragraph; and the situation is no different than if the stock he received had been preferred stock, subject to call at a price fixed.

Certainly, no one would contend that the Conservator or Liquidator of an insolvent insurance company would have to have the approval of the court to surrender preferred stock, which the court had authorized him to accept in exchange for other assets, upon that stock being called in accordance with its terms. When the court approved Rehab it approved a transaction by which the Conservator was obligated to dispose of the stock he received in exchange for the assets of Old Company in a certain manner and upon certain terms, and it thereby authorized him to consummate the transaction without further order.

If, however, it be assumed that the court must exercise the jurisdiction given it under Section 1037(d), it seems evident that the court did exercise that jurisdiction. Certainly, Rehab agreement involved assets of Old Company of a market value in excess of $1000; certainly the

DARK PA

provisions of paragraph 20 as to mutualization constituted a transaction involving the disposal of the only asset received by the Conservator in exchange for all of the assets of Old Company.

Petitioners argue, however, that, at the time Rehab was approved, the stock of New Company had no market value, and, therefore, they say the court could not then exercise its jurisdiction under 1037(d).

The answer to this argument is clear. In the first place, while the stock of New Company had no market value inasmuch as it was all held by the Conservator and as not subject to sale could have no market value, it did have an intrinsic value which could be measured approximately by the net worth of New Company. And certainly the statute does not preclude the court from giving approval of a transaction involving property which has no market value because not traded in but which has an intrinsic value in excess of $1,000. The court, in liquidation proceeding having acted in approving the transaction which is set forth in paragraph 20, exercised its jurisdiction under 1037(d) as well as under 1043.

This does not mean that the Commissioner was authorized by the court, or required by the rehabilitation agreement, to consent to any plan of mutualization that might be thereafter adopted by New Company and presented to him as the shareholder of that company. It only means that the court has approved his giving his consent to a plan of mutualization which conforms to the provisions of paragraph 20.

If the plan now presented does not conform to the provisions of that paragraph, then the Commissioner has not consented thereto and is not authorized to consent thereto, and the Commissioner had no jurisdiction to make the order in question. If it does conform, then the Commissioner has, by the terms of paragraph 20, given his consent to it, and the voting trustees are obligated by the terms of the trust to give their consent, which they have done.

If the plan does not conform to paragraph 20, then the voting trustees do not have power to consent, for the Con-

SE BLEED THRU

servator by vesting them with legal title could not vest them with any greater right to consent than he, himself, had, and he had no power to give and consent to any plan other than one conforming to the provisions of paragraph 20, without first securing court approval of his action. As to whether or not the present plan conforms to the provisions of Section 20 will be dealt with later.

Petitioners further contend that the Rehab did not, and the plan of mutualization does, constitute a disposal of the stock of New Company; that the mutualization agreement must, therefore, be approved by the court; that the Commissioner must, therefore, secure the approval of the court before he can consent to it.

This contention is answered by what we have already said. It is true that the mutualization plan is an agreement providing for the eventual sale of the stock of New Company, and that it provides for the present transfer of the legal title thereto to certain named voting trustees. But this agreement is a part, or, we might better say, the end result, of the transaction which was approved by the court when it approved paragraph 20 of the rehabilitation agreement.

Petitioners next contend that the order approving the Rehab agreement was void in that the court did not have before it a justiciable controversy as to the fairness, etc., of the plan of mutualization.

As heretofore pointed out, the court in the liquidation proceeding never had jurisdiction of a plan of mutualization as such, but it did have jurisdiction to determine whether or not the Commissioner should agree in advance to abide by a plan promulgated in accordance with the provisions of paragraph 20 of Rehab. It did give its approval of that transaction. It may have erred in so doing. It may have acted unwisely in so doing, but it had jurisdiction so to do, and its order cannot be attacked here.

Petitioners next contend that the court could not delegate its duty under 1037(d) to give or withhold approval of the price and the terms upon which the stock of New

DARK PA

Company could be disposed of by the Commissioner. The answer to this contention is that the court did not delegate its duty. Its duty was to approve or disapprove the Rehabilitation Agreement which included a transaction involving a disposition of New Company's stock; this duty it exercised.

The Petitioners contend that paragraph 20 of the Rehab agreement is void because thereby the Commissioner delegated his statutory power to determine the price and the terms upon which the stock of New Company should be sold. This contention, of course, is answered by the fact that the order adjudging the validity of paragraph 20 is now final, and the agreement is, therefore, not subject to attack in this proceeding. But, it is further answered by a consideration of the powers vested in the Liquidator by the statute. The powers granted to the Conservator by Section 1037 are very broad, and he is required only to have a court approval of the transaction involving property of the estate of a market value in excess of $1,000. He is empowered to deal with property in his hands upon such terms and conditions as he may deem proper, subject only to court approval in the instance above mentioned. Certainly, this power is broad enough to encompass a transaction by which he grants an option to buy at a price and upon terms of payment to be fixed by third person or persons.

It is true that the Commissioner acts as trustee, and it has often been held that a trustee may not enter into option contracts where the price and terms of payment are to be fixed by third persons, but in none of the cases which I have cited were the powers granted the trustees as broad as the powers granted the Liquidator by Section 1037.

Petitioners contend, however, that the Liquidator in the performance of his duties is declared by Section 1059 of the Insurance Code to be a public officer acting in his official capacity in behalf of the state, and from this they reason that in handling an estate in liquidation he is bound by the same strict rules as govern in the handling of public funds or property.

E BLEED THRU

This is not a proper conception of the meaning of Section 1059. The purpose of the Legislature in enacting 1059 and declaring that the Liquidator in the performance of his duties should be deemed a public officer, was to make it clear that in acting as a trustee of an estate in liquidation, he was still bound by the provisions of Political Code Section 4295 insofar as the provisions thereof are applicable. These provisions are now set forth in Sections 6100-04 and 6110 of the Government Code. The conclusion I have come to is made clear when one considers the large discretion and extensive powers granted a liquidator by Section 1037, to which I have already called attention. In exercising these powers he acts as trustee of a private trust, not a public trust. He handles, not public, but private funds and property. His acts affect not the public, but the policyholders, stockholders and creditors of a private corporation.

The petitioners contend that the Legislature could not have granted the Liquidator power to delegate the powers granted to him by statute, and that, therefore, the power to delegate his powers could not be given by contract. These questions, like all others attacking the validity of the rehabilitation agreement, are foreclosed by the finality of the order approving the validity of that agreement.

Petitioners contend that the Liquidator could not give his approval of the plan of mutualization until after its adoption by the directors of the Company. I think they are correct in this contention. However, by the terms of the rehabilitation agreement, he is obligated to give his consent, and equity will look upon that as done which ought to have been done.

Further, as the Conservator was bound to give his consent, so were the voting trustees, and they have consented. Ordinarily, voting trustees cannot give consent to the sale of stock, and thus destroy their trust, but where the trustor is bound to consent, and the trustees are so empowered, their consent binds him.

Here the voting trustees were obligated by the terms of the voting trust agreement to carry out the rehabilita-

DARK P

tion agreement, and as this agreement bound the Liquidator to vote the stock, so as to approve the mutualization plan—the reason which ordinarily requires the consent of the beneficial owner, to action by the trustees which will destroy the trust, is absent.

Petitioners next contend that the rehabilitation agreement is against public policy and void because it seeks by contract to mutualize New Company, contrary to the statutes as to mutualization of insolvent insurers.

They argue that New Company is but the alter ego of Old Company and but an agency of the Liquidator, and that, therefore, any proceeding for its mutualization must be had in accordance with the provisions of Section 1043-1062 of the Insurance Code. This contention is without merit.

On being appointed Conservator the Commissioner had the option of doing any one of four things: First, he could liquidate Old Company, or under Section 1043 of the Insurance Code, he could mutualize it, reinsure its business, or rehabilitate its business. He chose to do the last, and through it to accomplish partial reinsurance of the business of Old Company.

In carrying out his choice, he formed New Company and transferred all of the business of Old Company to it. After this transfer, Old Company ceased to be an insurer. It had no policyholders. It had no power to write insurance. It was merely a corporation that had been an insurer, in the process of liquidation. New Company was not, and is not, insolvent, and while under limited supervision of the Commissioner by the terms of the rehabilitation agreement, it is not now and never has been in his hands as Conservator or Liquidator. Since the approval and execution of the Rehab agreement, the Commissioner has not, either as Commissioner or as Conservator, or as Liquidator, possessed or had title to any of the assets of New Company. Rehab, and the order approving it, divested him of all right and title to the assets of New Company which had vested in him by the order appointing him Conservator.

GE BLEED THRU

No fraud is perpetrated by failure to pierce the alleged corporate veil of New Company, nor does recognizing it amount to a mutualization of an insolvent insurer through contract and in a manner not authorized by law.

New Company is a solvent insurer, and the only statutes that are applicable to its mutualization are the sections of Chapter 13, Division 2, Part 2 of the Insurance Code.

Petitioners further assert that the corporate entity of New Company must be disregarded and the agreement of mutualization treated as if it were one for the mutualization of Old Company, an insolvent insurer, because they say that if this is not done the Insurance Commissioner becomes a judge in his own case and is disqualified from acting pursuant to Sections 11526-7 of the Insurance Code.

The Commissioner as Liquidator has no personal interest in the property he holds. He is purely a statutory trustee. As such trustee he is a distinct juristic person from the person who acts as a statutory administrative officer.

Even if it be assumed that the Commissioner, acting as such, and the Commissioner, acting as Liquidator, is not two separate juristic persons, still the court should not pierce the corporate veil. The corporate veil is only pierced to avoid injustice. Here, if the veil were pierced and the New Company treated as insolvent, the effect of doing so would be disastrous. It is difficult to see how the corporation could be treated as insolvent and mutualized as an insolvent insurer without seriously affecting the transaction which it entered into as solvent insurer, without any approval of the court or commissioner.

Between the two situations, that of permitting the Insurance Commissioner to function as an administrative officer despite his interest as statutory trustee in the matter to be decided upon by him as Commissioner, and the evil that would result from treating New Company as an insolvent insurer, there can be but one choice.

The petition here alleges that certain members of the PDC have in the past had, through corporations or firms

DARK F

of which they were officers or members, business relationships with New Company, and that these relationships disqualified them to act as arbitrators (that is, members of PDC). Petitioners, by their briefs, have strongly pressed this matter.

The answer to their contention is threefold:

A. The parties, by Rehab, agreed that the appointing committee might choose the persons to act as members of PDC; they thus consented to the appointment of any person chosen in good faith by that committee, and no charge is made that it did not act in good faith.

B. The business relationships alleged (as admitted by the answer of New Company), are of such a character as would not, as a matter of law, disqualify the person from acting as a member of PDC.

C. No evidence was offered before the Commissioner upon this question, although the record shows that the Petitioners were then informed of the matters they now allege. The question is, therefore, not open for decision here.

What I have heretofore said disposes of all questions raised by the Petitioners, except two. These questions are:

First: Is the plan approved by the order of the Commissioner one such as is contemplated by the rehabilitation agreement and one, therefore, to which the Liquidator has, by the terms of the rehabilitation agreement consented?

Second: Are the findings of the Commissioner that the plan protects the rights of Old Company and its shareholders and that it will be fair and equitable in its operation, supported by substantial evidence in the light of the whole record?

I think both of these questions must be answered in the affirmative.

By the provisions of Rehab the parties submitted to PDC for determination the question of whether, in the

GE BLEED THRU

opinion of the Committee, mutualization was then (at the time of its report) practicable. The Committee has answered this question in the affirmative and unless their decision was arbitrary, the parties are bound by that decision.

Petitioners contend, however, that the plan proposed by the Committee in and of itself demonstrates that the Committee's decision that mutualization if "then practicable" was arbitrary because they say the plan does not provide either for the present consummation of mutualization or for a process of mutualization under which New Company is unconditionally obligated to buy and the shareholders unconditionally obligated to sell upon terms definite as to price and time of payment, but only provides for a process of mutualization under which the consummation of mutualization is dependent upon certain future contingencies.

Their point would be well taken if paragraph 20 of Rehab could only be interpreted as contemplating present consummation of mutualization or a contract which provided unconditionally for the purchase and sale of the stock of New Company by it upon terms definite as to price and terms of payment. Paragraph 20 is subject to the interpretation just stated and which Petitioners would place upon it, but that is not the only reasonable interpretation that may be placed upon it and is not the interpretation placed upon it by PDC or the Commissioner.

Paragraph 20 of Rehab, when taken by its four corners and viewed in the light of the circumstances that existed at the time of its approval by the Court in the liquidation proceedings and its execution by the parties, is reasonably subject to the interpretation that it contemplated the adoption of a plan of mutualization under which the consummation of mutualization might not only be delayed but might be contingent upon the happening of future events.

At the time Rehab was entered into the stock of New Company had no value and could not even have a potential value until such time as the operation of New Company

had indicated the probability that it could from its trust earnings make restoration of Non-Can benefits. The parties, by their agreement, therefore, postponed the time at which mutualization might be proposed by the policyholders for approximately ten years. By their contract they did not provide that at the expiration of ten years mutualization should take place, but only that a plan for mutualization might then be adopted, if, in the opinion of a price determination committee, it could then be adopted, having *due regard for the interest of all persons interested in New Company.*

The terms of paragraph 20 clearly indicate that the parties contemplated that the plan presented by the PDC might provide for an extended process of mutualization. The surrounding circumstances and undisputed facts show that they must have contemplated that the consummation of mutualization under any such plan might be defeated.

Paragraph 20 outlines the plan that may be presented by PDC. It provides that the plan shall specify not only the price but the terms of payment, shall name the persons by whom and the manner in which the right to vote the stock is to be exercised pending the complete payment of the price; that it may to that end provide for the creation of a voting trust and shall not only designate the initial trustees but make provisions for the appointment of their successor. It expressly provides that a plan may be adopted before the restoration of Non-Can benefits, but that in that event that "such mutualization" (that is the mutualization provided for by the plan) shall not affect the right of holders of Non-Can policies to the restoration of benefits as provided for in the agreement.

If the parties had contemplated that any plan promulgated by PDC should provide for the immediate consummation of mutualization, there was no reason to make provision for the stock to be held by anyone pending the payment of the price fixed. There was no reason for the appointment of voting trustees or for the appointment of successors to the initial trustees. It is evident that the

parties contemplated that PDC might present a plan which provided for a process of mutualization to occur at a future date. Further than this, the plan expressly contemplates the adoption of a plan before the restoration of Non-Can benefits, but it also provides that in proposing a plan the PDC were obligated to protect the interests of Old Company and its shareholders. It seems to follow that the parties must have contemplated that any plan adopted before the restoration of Non-Can benefits would of necessity have to defer consummation of mutualization until after that event for otherwise any amounts paid to New Company would, under the provisions of paragraph 19 of the agreement, have to be applied to the restoration of those benefits, thus depriving Old Company and its shareholders of any benefit therefrom.

Restoration of Non-Can benefits could only be made out of the corporate earnings of New Company. If a plan were adopted before the restoration of Non-Can benefits, the consummation of mutualization under the plan would of necessity have to be contingent upon the corporate earnings of New Company being sufficient to make restoration. It follows that the parties must have contemplated that such a plan might be defeated if the earnings of New Company were insufficient to accomplish restoration within the time limited by the plan.

I think the interpretation of paragraph 20 I have just indicated is a reasonable one, and that I, therefore, should not and can not substitute my judgment for that of the Commissioner and the PDC. I hold, therefore, that the plan presented and passed upon by the Commissioner is one contemplated by the Rehabilitation Agreement and is, therefore, one to which the Liquidator has consented, and that the Commissioner had jurisdiction to make the order under review.

Petitioners contend, however, that the finding of the Commissioner that the plan protects the interests of Old Company and its shareholders is not supported by substantial evidence. They say it was the duty of the Commissioner to make his own determination from evidence of

DARK F

the value of the stock of New Company at the date fixed by the plan for mutualization and to determine whether or not the price fixed was, in view of that value, a fair price. They say that the Commissioner did not have any evidence before him from which the value of the stock of New Company could be determined as of the date fixed for the acquisition of that stock by New Company and the payment of the price, and that therefore the Commissioner's finding is not supported by substantial evidence.

It is undoubtedly true that it was the duty of the Commissioner to determine whether or not the plan protected the interests of the shareholders of Old Company, but it does not follow that it was his duty in the present case to look behind the report of the Price Determination Committee and make an independent determination of the value of the stock and the fairness of the price. In the present case the shareholders, by paragraph 20 of Rehab, agreed that the price to be paid for the stock should be fixed by the Price Determination Committee, and agreed to dispose of the stock at the price and upon the terms it fixed, and the committee, having fixed a price and the terms of payment, the shareholder is obligated to accept that price unless PDC acted arbitrarily. (There is no question of fraud or gross mistake involved.)

As the plan presented gives to the shareholder the price for which he has agreed to sell, it protects him, and the Commissioner was bound to so find unless the evidence disclosed that PDC acted arbitrarily in fixing the price.

The Petitioners contend that PDC did act arbitrarily. They point out that under the plan mutualization will not in fact occur for approximately 25 years, and that the PDC did not fix, and had no facts before it from which it could fix, the value of the stock as of that time and that therefore it had no basis upon which to fix a price to be paid as of that time.

It must be conceded and Respondents do concede that neither PDC nor the Commissioner had any facts before them from which either the market value or the intrinsic

AGE BLEED THRU

value of New Company's stock could be determined as to the time fixed for consummation under the plan. PDC was not, however, charged with fixing the value of the stock as of the date of consummation, but charged with fixing a price to be paid as of that date. "Price" in its broadest sense is synonymous with "value," but in its narrower and more common sense it means the amount of money to be given in exchange for something else, and I think it is in that sense that the word is used in paragraph 20 of Rehab.

PDC did fix that price. It fixed it at $3,000,000 plus simple interest and in certain events, other augmentations. Unless it acted arbitrarily in so doing, its determination of the price to be paid is final and binding upon the parties.

An arbitrary act or decision is one "arrived at through the exercise of will or by caprice, one supported by mere option or discretion and not by a fair or substantial reason." (*Bedford Investment Co. v. Folb*, 79 Cal. App. 2d 363, at 366.) The committee's decision was not such.

The facts which the PDC had before it, as shown by the record here, were sufficient to uphold findings that: the present value of the stock was not in excess of $3,000,000; that if that value were now paid (and New Company could pay it now from its present capital and corporate surplus and still remain solvent), Petitioners could receive no benefit therefrom; that if all the future earnings of New Company were discounted at a reasonable rate, their present value would be an amount insufficient to restore Non-Can benefits, and that, therefore, even if that value were fixed as the price to be paid and New Company were in a position to pay it, still Petitioners could receive no benefit; that the right of Non-Can policyholders to restoration was a prior charge upon all corporate earnings of the Company; that a present value of $3,000,000 was only justified if the earnings of New Company were sufficient to enable it to complete restoration of Non-Can benefits by the middle of 1974.

On the basis of these facts it cannot be said that the committee acted arbitrarily and without substantial rea-

DARK P

son in fixing the price and terms of payment. The committee was dealing not with ascertained facts but with future probabilities. It of necessity had to recognize that there was no certainty that the earnings of New Company would be such as the committee, on the basis of all the presently known facts, calculated they would be. In order to protect the rights of Petitioners they had to defer payment until New Company had been able to make restoration of Non-Can benefits. If the Company were able to make such restoration prior to the middle of 1974 (the date indicated by the studies of PDC), then the present value of $3,000,000 was too low, and the committee provided for such an event by adding to that price an augmentation of $250,000 for each full year by which complete restoration antedated December 31, 1973. On the other hand, if New Company should be unable to make restoration of Non-Can benefits until after 1974, the present value of $3,000,000 is too high, for in fixing that value the committee had assumed that the shareholder would be entitled to all earnings after that date. In this latter contingency, however, the plan does not provide for any reduction of present value, but places the risk of it on New Company. The committee could with reason have treated the benefit thus given the shareholder as a further compensation for the delay in payment.

The committee of necessity had to take the situation of all parties and all of the facts and circumstances in consideration in fixing a price, and in view of this we cannot say that their conclusion as to the amount to be paid was not a rational one.

PDC might well have approached the problems presented to it and resolved those problems differently than they did. We may not agree with their approach or with their reasoning, but we cannot say, nor could the Commissioner say, that they acted without reason, and neither the Commissioner nor this Court can substitute his or its reasoning for that of the committee.

I have arrived at this last conclusion reluctantly because of the fact that all the shareholder presently re-

K PAGE BLEED THRU

ceives under the plan is a conditional promise to pay a sum of money at a distant date in the future and this promise has a present value, if the sum to be paid is discounted, for interest only, at 3%, much less than the sum which the committee finds to be the present value of the stock.

It follows that the petition for a peremptory writ of mandate must be denied and the alternative writ discharged. I find that the Commissioner had jurisdiction, that there was a full and fair hearing upon notice before him, and that his findings are supported by substantial evidence.

Counsel for respondents will prepare findings and judgment.

PAUL NOURSE,
Judge.

March 24, 1952.

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APPENDIX D.

Opinion and Decision of Insurance Commissioner

STATE OF CALIFORNIA
DEPARTMENT OF INSURANCE

In the Matter of
PACIFIC MUTUAL LIFE INSURANCE COMPANY, a California corporation.

OPINION AND DECISION

APPEARANCES:

GEORGE B. GOSE, ESQ., FRANK P. DOHERTY, ESQ., O'MELVENY & MYERS, by PAUL FUSSELL, ESQ., HOMER I. MITCHELL, ESQ., All of Los Angeles, California, For: Pacific Mutual Life Insurance Company.

FRANK E. SPAIN, ESQ., Of Birmingham, Alabama, For: Pacific Mutual Agency Association.

PAUL E. IVERSON, ESQ., Of Los Angeles, California, For: A group of Non-Cancellable Policyholders.

IRVING M. WALKER, ESQ., MARK MULLIN, ESQ., Of Los Angeles, California, For: Pacific Mutual Shareholders Protective Committee.

DONALD J. DUNNE, ESQ., Of Los Angeles, California, For: Harold B. Reed, a Non-Cancellable Policyholder.

J. R. GATEWOOD, ESQ., Of Dallas, Texas, For: Texas Stockholders.

KEROILLE HERVE, In propria persona.

G. R. COFOID, Of Los Angeles, California, For: Trust Department, Citizens National Bank, Guardian for George E. Meyer.

ALSO PRESENT:

HONORABLE GEORGE B. BUTLER, Life Insurance Commissioner and Chairman of the Board, Department of Insurance, State of Texas.

GE BLEED THRU

W. S. Hughes, Of Los Angeles, California.

Marshall Madison, Esq., Of San Francisco, California, As an observer.

Francis V. Nixon, Of Los Angeles, California, As an observer.

Members of the Staff of the
Insurance Commissioner of the
State of California,

Also Present:

H. A. Benjamin, Deputy Insurance Commissioner.
Charles Mehlman, Chief Actuary.
Frank J. Hogan, Field Actuary.

By the Commissioner

The Pacific Mutual Life Insurance Company of California (hereinafter called the "Old Company") is a California corporation. It was engaged in the life and disability insurance business for many years until misfortune overtook it in 1936. In 1918, or thereabouts, it had embarked upon a program of sale of policies of noncancellable accident and health insurance (hereinafter called "Non-Can"). It was this form of insurance that led to its insolvency, which resulted in its seizure by the Insurance Commissioner of the State of California in July, 1936.

Briefly, the non-can policies provided very broad disability indemnities for partial and permanent disabilities. With the exception of a few policies written just prior to the time the company was found to be insolvent, the non-can policyholders suffering permanent total disabilities became life annuitants with large indemnities under the terms of the contracts issued. The premiums on new policies were increased from time to time during the period this non-can business was written and the maximum benefits on such new policies were reduced during this time. Nevertheless, because all of the premiums at which the business was written were so low in comparison to the benefits granted,

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the company suffered huge losses. When reserves on the non-can business were required to be set up on a realistic basis, its capital and surplus were entirely wiped out and a very large deficit developed. The Old Company was thereupon taken over by the Insurance Commissioner in conservatorship, and shortly thereafter in liquidation. Under the law then and now prevailing, the Insurance Commissioner of the State of California is the conservator or liquidator in the event of such proceedings being taken against an insurer authorized to do business in the State of California.

The Old Company wrote life insurance on a participating basis and also on a non-participating basis. It also wrote a very substantial volume of accident and health insurance on a non-participating basis. The assets devoted to the participating life business written by the Old Company were held separate and apart from the other assets of the company and, for most purposes, it can be said that this department was, in effect, a mutual company operated within the corporate framework of a stock insurer.

The Insurance Commissioner, at the time of the conservatorship, caused a new corporation to be formed, called Pacific Mutual Life Insurance Company (hereinafter called the "New Company"), under the laws of the State of California. Capital and surplus for the New Company were provided from the surplus of the Participating Department of the Old Company. The Commissioner, as Conservator, was the purchaser of the stock. The New Company fully reinsured all of the life insurance policies and all of the accident and health insurance policies of the Old Company, other than the non-can policies, under the terms of a reinsurance and rehabilitation agreement which becomes all-important in this proceeding. This agreement is hereinafter called the "Rehabilitation Agreement." Opportunity was given at that time for life and accident and health policyholders of the Old Company to refuse this reinsurance and file their claim against the Liquidator. A small number, only, of such policyholders ever filed such claims. Nearly all of them accepted the reinsurance in the New Company.

GE BLEED THRU

The non-can policyholders were given the option of accepting partial reinsurance or filing their claims against the Liquidator. Most of the non-can policyholders accepted the limited reinsurance and a relatively small number filed their claims. The earliest policies issued by the Old Company, because of the tremendous rate or premium deficiency pertaining to such policies, were reinsured to the extent of 20% only; the remainder were reinsured to a greater extent. The last group of such policies to be issued, wherein the rates charged and the benefits promised were on a more realistic basis, were reinsured to the extent of 90%.

The Rehabilitation Agreement provided that there should be restored to the non-can policyholders from time to time, out of certain of the profits of the New Company, the Benefits which were not reinsured. Under the terms of the agreement, the company was left free to make such restorations as it considered proper out of certain of its profits which are hereafter described, in any year other than a year in which the company was regularly examined by the Insurance Commissioner. In the years in which the company was so examined, the Commissioner was given power to require restorations out of earned surplus of the so-called Corporate Department of the New Company to such extent as he thought reasonable.

The New Company was separated into several departments—the Participating Department, the Non-participating Department, the Accident and Health Department, and what was called the Corporate Department. The Participating Department was and is, in effect, a mutual life insurance company run within the corporate structure of the New Company, its assets being separated from the remaining assets and surrounded with safeguards maintained to prevent them from being used for the benefit of any but the Participating policyholders. The profits of this Department on business written directly by the New Company were not available for the restoration of the non-can policies under the terms of the Rehabilitation Agreement. 10% of the profits of the old (reinsured)

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Participating business under the terms of the Rehabilitation Agreement were available for restorations of the non-can business.

The so-called Corporate Department was really not a department at all, but was an accounting device set up to account for or hold the profits and surplus of the Non-participating Department, the Accident and Health Department and the 10% of profits of the reinsured participating business, referred to above.

It is obvious that the New Company was formed to prevent the tremendous loss that would have been incurred by all policyholders if it were necessary completely to liquidate the Old Company without any reinsurance.

Shortly after the New Company was formed and the Rehabilitation Agreement was executed, legal title to the stock was transferred to a group of voting trustees under the terms of a voting trust agreement. The trustees under the terms of this agreement voted the stock and thus controlled the New Company. The Insurance Commissioner, as Liquidator of the Old Company, however, retained, and still retains, the beneficial interest in such shares.

Since 1936 the New Company has been reasonably prosperous and as of the end of 1948 restorations of 24% had been made upon the originally uninsured portions of the non-can policies. Presently, a total of 36% has been restored. The Rehabilitation Agreement provides that simple interest at the rate of 3½% per annum shall be paid upon such restorations at the time they are made. The restorations made represent a very large sum of money.

The Old Company is a party to the Rehabilitation and Reinsurance Agreement because it was executed by the Commissioner as Conservator thereof. The agreement recognizes a contingent interest of the Old Company in the New Company. It also recognizes a right of the policyholders of the New Company to propose that any or all of its departments be mutualized if possible, and made provision for a method of arriving at a plan for mutualization if it was found, by a committee provided for in the

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Rehabilitation Agreement, to be feasible. It also recognizes that the stock of the New Company may be sold if it becomes necessary for the protection of the estate in conservation or liquidation, the New Company or its policyholders. This sale can be made only after a proper showing of the necessity for such sale and a full hearing thereon.

These provisions are contained in Section 20 of the Rehabilitation Agreement, and since that section of that agreement is of paramount importance in the determination of this matter, that section of the agreement is set forth at length as Part I of the Appendix to this Opinion and Decision.

Pursuant to the provisions of Paragraph (a) of Section 20, and within the time allowed for such action, the required number of holders of Participating policies of life insurance requested the New Company to create an Appointing Committee with a view to a possible voluntary mutualization of the New Company. The Appointing Committee duly appointed a Price Determination Committee as provided in said Section 20(a). The members selected were:

Mr. Horace R. Bassford, Vice President and Chief Actuary of Metropolitan Life Insurance Company

Mr. Albert J. Hettinger, Jr., a partner of the firm of Lazard Freres

Mr. Ray D. Murhpy, Vice President and Actuary, of Equitable Life Assurance Society

Mr. A. J. McAndless, an actuary by profession, and President of Lincoln National Life Insurance Company.

This committee accepted the appointment and elected Mr. McAndless chairman thereof. The committee entered upon its deliberations and after long and extensive studies rendered its report on April 4, 1950.

Thereafter, pursuant to the provisions of the Rehabilitation Agreement, the plan was submitted to all life policyholders of the New Company, who, by the required vote,

requested that it be submitted. The plan was thereupon submitted to the Insurance Commissioner of the State of California for his examination, pursuant to the provisions of Section 11527 of the Insurance Code of this State. That section reads as follows:

> "11527. The commissioner shall examine the plan submitted to him under the provisions of subdivision (c) of Section 11526. He shall not approve such plan unless in his opinion the rights and interests of the insurer, its policyholders and shareholders are protected nor unless he is satisfied that the plan will be fair and equitable in its operation."

A public hearing was held in order to determine the questions required to be determined by the provisions of that section. The hearing went on for many days. Abundant testimony was taken, and documentary evidence was also submitted. The case was ably and thoroughly argued by counsel for the various interested groups.

The Price Determination Committee found that mutualization was feasible and formulated a plan for such mutualization. It found that the plan adequately protects the rights and interests of the New Company, of each class of its policyholders, and of all interests represented by the Insurance Commissioner of the State of California as holder of the beneficial interest in the stock of the New Company, and further found that the plan would be fair and equitable in its operation and that it could be practicably accomplished, having due regard to the interests of all persons interested in the New Company.

A copy of the plan for voluntary mutualization presented by that committee, excepting the voting trust agreement, is attached as Part II of the Appendix to this Opinion and Decision.

Greatly epitomized, the plan determined that both the Participating and Non-Participating Life Departments of the company should be mutualized by the purchase and cancellation of all of the outstanding shares of capital stock of the New Company, thus converting the New Com-

pany into a non-stock insurer conducted for the benefit of its members who shall be the policyholders of the participating and non-participating life classes.

The price to be paid for the outstanding shares is to be three million dollars with simple interest in each calendar year at the rate paid on the furthest maturity of United States Government bonds publicly held and quoted at the end of the preceding calendar year. This purchase price is to be augmented by the sum of two hundred fifty thousand dollars for each full calendar year by which the date of completion of restoration of non-can benefits antedates December 31, 1973. The same rate of interest under the plan will apply to the augmentations in price subsequent to the completion of restoration.

The plan provides for the accumulation of a fund to be used in partial payment of the purchase price and interest, by setting aside a special surplus fund of 5% of the net profits before dividends of the Participating Department exclusive of the profits from contracts reinsured under the Rehabilitation Agreement. This special surplus fund shall have interest upon it set aside in the fund at the same rate as interest is to be paid on the purchase price.

The purchase price is to be paid only after completion of full restoration of the non-can policies and when the fund standing in the special surplus fund plus the capital and surplus in the general corporate accounts equal or exceed the price plus interest. The financial condition of the corporation also has to be such that after the payment, as aforesaid, the company shall have admitted assets in excess of its liability amounting to 4% of its admitted assets plus 25% of the premiums collected during the preceding calendar year on all one-year term group insurance business and on all accident and health insurance. The plan provides for a method of bookkeeping with respect to the special surplus fund and the effect of payment of the purchase price of the shares.

The plan also provides that the present method of restoration of non-can benefits, as set forth in the Rehabilitation Agreement, shall be continued.

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Upon the acceptance by the policyholders of the plan, the present voting trust agreement shall be terminated and the legal title to the shares shall be held, pending the payment of the purchase price and cancellation, and shall be voted by another group of voting trustees named in the plan. The plan provides that it shall be the policy of the New Company to write at least half of its new life insurance other than group insurance each year in the Non-Participating Department. It provides for the doing of all acts necessary legally to accomplish the mutualization upon payment of the purchase price, and for the cancellation of the shares. It provides for an effective date of the plan and what shall be done in the event that it is impossible to consummate the mutualization of the New Company, and for the interpretation of the language in such a way that the provisions of the Rehabilitation Agreement shall be carried out.

CONTENTIONS OF THE VARIOUS PARTIES

The New Company itself was an active proponent of the plan at the hearing, as was an association of its general agents. Both the company and this association contended that the plan properly protects the rights and interests of the New Company, its policyholders and its shareholders, and that the plan would be fair and equitable in its operation.

The plan was opposed by an association of stockholders of the Old Company, which was called Pacific Mutual Shareholders Protective Committee (which is hereinafter referred to as the "Shareholders"), by a policyholder of the company, and by a group of non-can policyholders. Those who opposed the plan are hereinafter sometimes called protestants.

A letter, purporting to be an offer, was presented by American National Insurance Company, of Galveston, a large life insurance company, offering to purchase the stock of the New Company from the Commissioner, as Liquidator, for three million dollars. That company also offered to agree to restore benefits on non-can policies by

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the use of profits of the New Company or, if they proved insufficient, within seven years, out of its own funds. It also contained other stipulations which are unimportant here. It was received in evidence because it bore upon the reasonableness of the purchase price determined by the Price Determination Committee for said shares. Under the terms of Section 20(d) of the Rehabilitation and Reinsurance Agreement, this offer of purchase could not be accepted as the basis of a contract for the purchase of such shares, however, because such shares cannot be sold unless it is found that conditions are such as to require such a sale of stock for the protection of the estate in liquidation, the New Company or its policyholders. No such finding is possible on this record because it affirmatively appears that the New Company is in a prosperous condition and there is no evidence of any of the other conditions that would allow the sale of the stock to other persons.

A period of more than fourteen years has elapsed since the Old Company was seized. During that time it has not been able to avail itself of funds sufficient to restore the non-can benefits, as provided in Section 20(c) of the Rehabilitation Agreement, although the record shows that some attempts were made by the Shareholders to finance such a restoration. It was the contention of the Shareholders at the hearing that the Old Company had been unable to arrange for the financing of such restoration because of the option for mutualization on the part of the policyholders set forth in Section 20(a) of the Rehabilitation Agreement. Its counsel earnestly urged that as long as the option to mutualize was in existence or in the process of accomplishment, it would be impossible for the Old Company to obtain funds with which to make the restoration; that since it was faced with this impediment to such financing, it became the duty of the Commissioner to disapprove the first plan of mutualization offered, whatever it might be, in order to free the Old Company of this impediment to financing the restoration. This contention is without merit. The Old Company was a party to the Rehabilitation contract and is bound by its terms. The impediment, if such it can be called, was in the contract at

DARK P

the time the Old Company became a party to it, and it cannot now be relieved of the bargain it made simply because it contends it was a hard one.

It was contended by protestants that the intent of the Rehabilitation Agreement had been thwarted by the management of the New Company with the acquiescence of several of the individuals who had held the office of Insurance Commissioner since the time the Rehabilitation Agreement was executed. It was argued that the management of the New Company and the Insurance Commissioner had allowed the New Company to accumulate unreasonable surplus out of profits which should have been used for restoration, and that as a result, restoration has been impeded and the amount of benefits restored at the present time is considerably less than should have been restored had the profits been used for restoration rather than applied to the surplus account of the company.

This contention involves a question of judgment on the part of the management of the New Company and of the several persons who have occupied the Insurance Commissioner's office during the period of the New Company's operations. It is a point that cannot be settled in this proceeding, because it involves a question of the exercise of discretion.

If a life insurance company is to make profits, it must be kept prosperous and maintain a financial condition which will command the confidence of the insuring public. The life insurance business is a highly competitive one. Purchasers of life insurance endeavor to buy it in strong companies which are showing progress and whose capital and surplus in relation to its business in force compares favorably with that of its competitors. One of the principal methods used by life insurance agents in demonstrating to their prospective customers the strength of the companies they represent as contrasted with competitive companies, is to compare the relationship of surplus and voluntary reserves to admitted assets. If their company has a higher percentage relationship than the competitive company, it is evidence that their company is somewhat

GE BLEED THRU

stronger. Likewise, agents point out to their prospects that this percentage relationship is increasing, rather than remaining static or diminishing, if they can, in attempt to show that their company is increasing its strength as time goes on. If the New Company had not been allowed to maintain a position in this regard, at least somewhat similar to that of other life insurance companies similarly situated, its business would not have expanded, it would not have been prosperous, and without being prosperous it is obvious that restorations would have been greatly impeded. To use all of the profits of the New Company for restoration would have been only to call into play the ancient aphorism of killing the goose that laid the golden egg.

The evidence demonstrates that the surplus of the company has been allowed to grow and that the ratio of surplus to admitted assets has increased since the New Company began its operations. Whether the surplus should have been allowed to increase at a rate less than that which it has increased, is a question of judgment and discretion. If the management of the New Company, or the Insurance Commissioner, has abused that discretion, the remedy of protestants is not in this proceeding, but is in a proceeding in Court.

Protestants further contend that if the plan of mutualization is approved, the New Company would have an interest in deferring restoration payments, in order to minimize the amount which eventually would have to be paid for the stock of the company. The plan of mutualization does not in any way affect the provisions of the Rehabilitation Agreement with respect to restoration. The New Company is still bound to make restoration with reasonable dispatch and the Insurance Commissioner is enjoined by the terms of that agreement to see that any funds in excess of those reasonably needed by the New Company should be applied to restoration at the time when the company is officially examined. It must be assumed that future Insurance Commissioners will perform their duty in enforcing the terms of the Rehabilitation Agreement.

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The Price Determination Committee has estimated that full restoration will probably be accomplished in about twenty-five years from the end of 1948. These protestants contend that restoration by this method will be too slow, that it is contrary to the intent and spirit of the Rehabilitation Agreement, and that by the time full restoration is made, many—if not most—of the non-can policyholders will be dead. It is contended that if the mutualization plan is found not to meet the requirements of Section 11527 of the Insurance Code, other means may be found by which restoration can be completed much sooner than is contemplated by the authors of the plan of mutualization.

While restoration has been and remains a paramount consideration under the Rehabilitation Agreement, it must be remembered that when the policyholders of the Old Company, including the non-can policyholders, accepted reinsurance in the New Company, they became parties to novations and such policyholders bound themselves to accept the terms of the Rehabilitation Agreement. The non-can policyholders, by accepting such reinsurance, bound themselves to accept restoration in the manners contemplated by the Rehabilitation Agreement and in no others.

The contentions of protestants to the effect that the mutualization plan should not be approved, in order that other and more expeditious means of restoration might be developed, are not convincing. In the first place, there is no assurance that any better plan could be worked out and it is to be noted, again, that no such plan has been developed in something over fourteen years. In the second place, the provisions and safeguards contained in the Rehabilitation Agreement with respect to restoration are not in any way affected by the plan and, as stated above, non-can policyholders are not entitled as a matter of right to any other methods of restoration.

It should be noted that the twenty-five year estimated period for full restoration is only an estimate. It is in no way binding on the Commissioner or on the company. Both will still have the duty to see that restoration is accomplished at the earliest date possible, consistent with sound judgment as to the company's financial position.

GE BLEED THRU

Protestants contend that the plan does not meet the terms of the Rehabilitation Agreement because it provides for mutualization only of the Life Departments of the company with such departments controlling the Accident and Health Department as a proprietorship. This contention is answered by an understanding of what mutualization means. It means, according to the Insurance Code, Section 11525, the acquisition of the stock of a company by its policyholders for the benefit of its policyholders, or any class or classes thereof. The whole section reads as follows:

> "11525. A solvent domestic incorporated insurer having a paid-in capital represented by outstanding shares of capital stock and issuing, on a reserve basis, nonassessable policies of life insurance or of both life and disability insurance, may convert itself into an incorporated mutual life insurer, or life and disability insurer, issuing nonassessable policies on a reserve basis. To that end it may provide and carry out a plan for the acquisition of the outstanding shares of its capital stock for the benefit of its policyholders, or any class or classes of its policyholders, by complying with the requirements of this chapter."

The plan falls within this definition and therefore this contention of protestants is without merit.

Protestants further contended that the plan was unfair to the life policyholders of the New Company, particularly the participating policyholders thereof, because they, at the present time, are true mutual policyholders in that the Participating Department of the company is separate and apart from the other departments of the company and the assets thereof cannot be touched excepting for the benefit of the participating policyholders. It was pointed out in this regard that the original capital and surplus funds of the New Company were provided by the Participating Department of the Old Company and that a percentage of the profits of the old participating business is available under the terms of the Rehabilitation Agreement for restoration. The plan provides that funds for payment for the

stock under the plan must be provided by the profits of the Participating Department. This contention of protestants therefore requires serious consideration because, at first glance, at least, it appears to have very considerable merit.

With respect to the old participating policyholders, it was frankly stated by one group of proponents of the plan that mutualization as to the old participating policyholders would be of value to them mainly on a psychological basis, in that the turmoil surrounding the New Company and its predecessor would be ended. Thereupon, its agency force would overcome sales resistance because of a stabilization of the New Company's future. Also, all participating policyholders ultimately would have the benefit of the profits of the Accident and Health Department of the company, if any there were. These same considerations applied to the new participating policyholders who, as a class, are probably younger and hence have a better chance of surviving the time when full mutualization is accomplished.

The advantage of the plan to the non-participating policyholders is quite obvious in that they will ultimately become, if the plan is successful, proprietors of the company along with the other participating policyholders, and will not have to make payment for this interest. It should be remembered, in this regard, that Section 11527 does not require a plan of mutualization to be shown to be to the advantage of any particular class or classes of policyholders.

The accumulation of the fund for payment of this purchase price is restricted to a sum of 5% of the profits of the Participating Department, before dividends to policyholders. It is well-known that mutual life insurers do not pay or return all of their profits to their policyholders as dividends, but customarily retain some portion of such profits, or as they are sometimes called, excess premiums, as additional surplus for additional protection to policyholders. This fund, by the terms of the plan, is still the property of the Participating Department, and a part of

its surplus. When payment for the stock is made, and the company is mutualized, the general surplus of the New Company would be more directly available for the benefit of participating policyholders, and therefore there should be less need for a separate participating surplus than before. In any event, provision is made for return of monies paid from this fund. Thus, it is extremely unlikely that the 5% accumulation would in any way affect the dividends to the participating policyholders.

As has already been pointed out, restoration from profits as contemplated by the Rehabilitation Agreement will in no way be affected by mutualization, and if the evidence and contentions of the association of general agents of the company who appeared as proponents of the plan are believed, restoration may be hastened by adoption of the plan because it would be easier to sell insurance when all turmoil over control of the New Company is put to an end and the company embarked upon a business course on an even keel without threat of further business storms.

Protestants contended that the real advantage of this plan would be to the management of the New Company and that, it was said, it is well known that managements of mutual insurance companies tend to perpetuate themselves. This contention also is without merit. That there have been abuses in the mutual insurance field, on the part of managements perpetuating themselves, cannot be seriously questioned but the same can be said of abuses of management of all business corporations. Mutual policyholders are analogous to stockholders in many respects. It is well known that stockholders frequently are not diligent in protecting their rights in corporations in which they own the proprietary interest. They fail to attend stockholders' meetings or properly to interest themselves in the corporation's affairs. The law provides remedies for the abuses mentioned and if a stockholder wishes to avail himself of such remedy, he can do so. The law likewise gives such remedies to mutual policyholders. If they sleep upon their rights, they have no one to blame but themselves. It cannot fairly be said that because there have been abuses in the past in the perpetuation of manage-

DARK F

ment of some mutual insurance companies, that such will be the case with respect to the company here involved. If such abuses should ever develop, it behooves the policyholders to remedy the situation in the manner provided by law for that purpose.

The contention is made by the Stockholders, particularly, and to a certain extent by the other protestants, that the value placed upon the stock by the Price Determination Committee and incorporated in the plan by them is unreasonably low. There was abundant evidence to support the findings of the committee as to the price of three million dollars, both upon the basis of a price to be paid for nonparticipating life insurance in force and upon other bases.

In arriving at the estimate of the value of the stock, the committee made a detailed study and estimate of the probable earnings of the New Company. Upon the basis of this estimate and assumed discount rate, the value of the stock was mathematically determined. The committee likewise considered the value of the business from the standpoint of the market value of other insurance securities and from the standpoint of a valuation upon the usually accepted empirical basis of the proprietary business of the company. Upon both of these bases, the value of the stock would be nil. Upon consideration of the three bases and in the exercise of their judgment, the committee arrived at a minimum price as of December 31, 1948, of three million dollars.

While from a purely mathematical standpoint, some question may be raised as to the discounting to 1948 of future earnings applicable to the stock at a 10% annual rate, while the interest on the augmentations would be at a much lower rate, still it must be remembered that the determination of price by the committee was not on a mathematical basis, but involved many other considerations. The evidence is uncontradicted that during the period of nearly fourteen years no one has come forth with funds to make these restorations in any manner countenanced by the Rehabilitation Agreement. There is evidence that at times the Stockholders had in mind various plans for making

GE BLEED THRU

these restorations, but it was pointed out that these arrangements were unsound in that they could not be countenanced by sound insurance accounting practices enforced by state authorities, who regulate the insurance business.

One of the methods suggested was the issuance of notes to non-can policyholders in payment or partial payment of their claims for restoration benefits. Such notes would have to be listed on the balance sheet of an insurer, under recognized insurance accounting practices, as liabilities of the company and thus the surplus of the company would be reduced by the amount of these notes. A financial expert, a member of the Price Determination Committee, gave a great deal of opinion evidence to the effect that securities could not be sold to the public to obtain sufficient funds to make the required restorations. These opinions of this expert have been corroborated to the extent that no one has been able to arrange for the sale of securities during the 13½ years or thereabouts that the opportunity has been present under the terms of the Rehabilitation Agreement. The only evidence that might tend to show that the price fixed was too low was the offer of American National Insurance Company hereinabove referred to. It is significant that the amount offered for the stock by that company was three million dollars, too. In addition, the offer promised full restoration within seven years, which is, in legal contemplation, a better offer than the promise contained in the Rehabilitation Agreement to make the restorations out of profits or by the other methods therein contemplated, inasmuch as one is a definite promise as to time of performance and the other is indefinite and subject to the contingencies. However, as was pointed out above, this offer was one that could not be entertained under the terms of the Rehabilitation Agreement.

It should be remembered that the plan provides for augmentation of the purchase price in the event that the New Compay is sufficiently prosperous to complete restoration prior to the 25-year period from December 31, 1948, and that, in the event restoration cannot be completed by December 31, 1983, the plan will by its own terms fail. These augmentations were incorporated into the plan

because the determination of the time of restoration would depend upon the degree of future success enjoyed by the New Company, which cannot be forecast with accuracy. Therefore, the three million dollar figure was set up as a minimum price. If the company proves quite prosperous, the Old Company will participate in this prosperity to some extent. Arrangements of this kind are quite common in the business world. Leases, for instance, are frequently entered into which state a fixed minimum rental, to be augmented by a percentage of the lessee's gross receipts if the percentage exceeds the minimum. Thus, the lessee participates to a certain extent in the future worth of the premises, if the future proves they become more valuable. Other business examples are not hard to find. The plan of augmentation is sufficiently analogous to these cases drawn from the business world to make further discussion as to the reasonableness of this arrangement for augmentation unnecessary.

As was said before, it was contended by protestants that mutualization of the New Company benefits no one except the management and that the plan, therefore, should not be approved. This contention is based to a large extent upon the fact that the normal benefits of mutualization, that is, the participation in the profits of the operation of the New Company, would not become available for such a long period of time that many of the present policyholders would be dead.

It is to be understood that in almost every mutualization proceeding a long period of time elapses between the development of a plan for mutualization and its ultimate consummation. This fact was as apparent in 1936 as it is at this time. Nevertheless, the Rehabilitation Agreement, which sets forth the rights of the parties herein involved, plainly contemplates mutualization at any time after July 1, 1946, and likewise contemplates that a plan may be developed for mutualization prior to the completion of the restoration of non-can policies. All of such mutualization proceedings must necessarily be viewed as long term operations and for the general benefit of the policy-

RK PAGE BLEED THRU

holders of the company being mutualized, in a broad and over-all sense.

Protestants, particularly the group of non-can policyholders, contended very strongly that the plan could not be found to meet the requirements of Section 11527 because it would freeze the method of restoration of the non-can policies to restoration from profits alone. It was pointed out by them that the non-can policyholders, under the terms of Section 20 of the Rehabilitation Agreement, now have at least a hope that the funds necessary for immediate restoration may be raised by the Old Company.

It cannot be gainsaid that if the plan goes into effect, it will have the effect of freezing the method of restoration as protestants contend. But the non-can policyholders, by accepting reinsurance in the New Company, agreed to all of the terms of the Rehabilitation Agreement and, as has heretofore been pointed out, the Rehabilitation Agreement grants what is in effect an option on the part of the policyholders of the New Company to mutualize. The non-can group cannot now be heard to complain that the effect of the carrying out of this option may freeze the method of restoration to restoration from profits. They made their bargain and as is the case with the Old Company, they cannot now complain of the carrying out of that bargain simply because they do not like it.

It was earnestly contended by the Shareholders that if the plan is approved and adopted, the Insurance Commissioner loses control over restoration. In this regard, it was said that some of the functions that belong to the Insurance Commissioner would be delegated to the voting trustees under the terms of the plan. The answer to this is that the plan does no such thing. The plan cannot and does not amend the Rehabilitation Agreement. As has been noted above, restoration is still a paramount obligation of the New Company and it is the duty of the Commissioner under that agreement to see that restoration is completed with dispatch.

It was also stated that since the voting trustees under the plan were enjoined to see that the company maintained

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a balance of writings in the Participating and Non-Participating Departments, that this was another delegation of power that belonged to the Commissioner. The answer to this is that although the voting trustees are required to see that such a balance is maintained, a provision of the Rehabilitation Agreement makes the same requirement. The Commissioner still retains full power to enforce all terms of the Rehabilitation Agreement by requiring restorations to be made.

It was contended by the Shareholders that the committee was prejudiced, because it felt that non-can policyholders had made an unconscionable bargain in obtaining their non-can policies in the first place, because the premiums were grossly disproportionate to the benefits granted. There is some evidence that at least one of the members of that committee did feel that such policyholders had made an unusually good bargain, but since the plan did not alter the rights of the non-can policyholders with respect to restoration, that view is of no consequence. There was no evidence that the committee in determining the price of the stock was influenced by the fact that non-can policyholders had made unusually good bargains in purchasing their insurance. It was recognized by the committee that the contracts must be carried out regardless of the nature of the bargains.

FINDINGS

IT IS HEREBY FOUND AS A FACT that the rights and interests of the New Company, its policyholders, and the holder of its shares are protected under the terms of the plan hereinabove referred to, and that the plan will be fair and equitable in its operation.

CONCLUSIONS OF LAW

IT IS HEREBY CONCLUDED that the plan is lawful in all respects and meets all requirements of the Insurance Code. The plan is therefore hereby approved.

Dated at Los Angeles, California, September 22, 1950.

WALLACE K. DOWNEY,
Insurance Commissioner of the State of California.

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"(20) Neither the Conservator, nor, if one be appointed, the Liquidator, of the Old Company, shall dispose of any of the stock of the New Company except as follows:

"(a) At any time between July 1, 1946, and January 1, 1948, and thereafter so long as the Conservator or a Liquidator of the Old Company may continue to hold any or all of said stock, ten percent (10%) of the holders of participating policies of life insurance entitled to vote at a policy holders' election on a proposal for voluntary mutualization of the New Company, whether those reinsured hereunder or those issued by the New Company (each policy holder for this purpose being regarded as one person regardless of the number of policies owned or amount of insurance held) may request the New Company to create an Appointing Committee as hereinafter provided to exercise the duties and functions hereinafter specified in respect of a proposed voluntary mutualization of the New Company, in accordance with the laws of the State of California in effect at the time of said request, or, if said laws then so permit, of any one or more departments thereof. Such request shall specify the department or departments of the New Company desired to be mutualized.

"Upon the receipt of such request the New Company shall create an Appointing Committee consisting of the then President of the Association of Life Insurance Presidents, the President of Leland Stanford Jr. University, and the Provost of the University of California at Los Angeles, or persons occupying similar positions if their or any of their titles shall have been changed. In the event any one or more of such persons shall refuse or be unable to act, the remaining member or members shall fill the vacancy or vacancies thereby created by their appointment in writing of another person or persons of similar position and standing. If all of said persons refuse or are unable to act, the Court or any Judge thereof shall, on the application of the Commissioner, designate an Appointing Committee consisting of three (3) persons of similar position and standing. Said Appointing Committee acting through not less

than a majority of its members, shall designate a Price Determination Committee of not less than three and not more than five (5) persons skilled in matters of insurance company valuation, which committee, acting through not less than a majority thereof, shall determine whether in their opinion the proposed voluntary mutualization of the New Company, or of the Department or Departments thereof specified in said request can then be practicably accomplished, having due regard to the interests of all persons interested in the New Company. If it be determined that such mutualization is not then practicable, no further steps shall be taken in connection with a possible mutualization of the New Company under the provisions of this subparagraph until at least six months after the date of such determination. If in the opinion of a majority of the members of the committee such mutualization is then practicable, the committee shall determine the proper price to be paid upon such mutualization and appropriate terms of payments thereof; said determination shall not be made, however, prior to January 1, 1947.

"If, at the date of the appointment of such committee the New Company shall have in force Participating Life Insurance written subsequent to the effective date of this agreement in an amount in excess of its Non-Participating Life Insurance written during the same period, one-half (½) of such excess shall, for the purpose of fixing the proper price to be paid (but for no other purpose) be deemed to be, and shall be valued as, Non-Participating Life Insurance. If at the time of such appointment, there shall have been transferred from the Participating Department in accordance with the provisions of subparagraph (d) of paragraph 6 hereof, less than ten percent (10%) of the then accrued earnings described therein, or if there shall have been transferred to the Participating Department any working capital pursuant to the provisions of subparagraph (c) of said paragraph 6, any unpaid balance thereof shall, for the purpose of fixing the proper price to be paid (but for no other purpose) be deemed to be a debt then due and matured. Said Committee shall in its report to the New Company include a plan of mutualization of

the New Company, or of the department or departments thereof specified in said request of the policy holders. Such plan shall specify, in addition to any other relevant matters, the price to be paid, the terms of payment, and the persons by whom and the manner in which the right to vote the stock of the New Company is to be exercised pending complete payment of the purchase price. In this connection the said Committee, if it deem it advisable, may provide in the plan for the creation of a voting trust, designate the initial trustees, and make provision for the appointment of their successors. Unless the benefits under Non-Can Policies have theretofore been fully restored and claims against the Liquidator fully paid, such plan shall further provide that such mutualization shall not affect the provisions of paragraph 17 or of paragraph 14 hereof or the right of holders of Non-Can policies to the restoration of benefits from the sources and in the manner therein provided.

"The New Company agrees that within sixty (60) days after the making of such report (unless said report shall be to the effect that mutualization is not then practicable) it will mail copies thereof to all of its policy holders entitled to vote upon such plan or plans of mutualization if submitted according to law. If within one hundred twenty (120) days after the mailing of such notice, ten percent (10%) of the policy holders entitled to vote upon any such plan or plans (each policy holder being for this purpose regarded as one person regardless of the number of policies owned or amount of insurance held) shall request in writing the submission thereof, the New Company will promptly submit the same in accordance with the laws of the State of California then in effect. The Conservator for himself and for any successors in the ownership of said stock claiming under him in any manner other than through a sale of said stock pursuant to the provisions of sub-paragraph (d) hereof agrees to consent and hereby consents as the holder and owner of the stock of the New Company to such plan of mutualization. In the event said mutualization plan is adopted, the Conservator, or a Liquidator as aforesaid, shall dispose of such stock in accordance with such plan.

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The expenses of the foregoing proceedings including costs, fees and expenses of the Price Determination Committee, shall be borne by the New Company; and, unless the proposed plan of mutualization is consummated, shall be charged to the Participating Department thereof.

"In the event the Price Determination Committee has been appointed as herein provided prior to January 1, 1948, said Committee shall have the power to extend the time within which mutualization may be effected hereunder for such period or periods of time as it may deem necessary for the orderly completion of mutualization proceedings as herein provided.

"(b) If at any time prior to the expiration of the option to mutualize a plan of merger, consolidation, reorganization or reinsurance of the New Company is presented to the New Company, or to the Conservator or Liquidator, which in the opinion of the Board of Directors of the New Company cannot be consummated without the elimination of the provisions for mutualization herein contained, the New Company may create an Appointing Committee in the same manner as though the proceeding were under subdivision (a) of this paragraph. Said Committee, acting through not less than a majority of its members, shall designate a committee of not less than three nor more than five persons, skilled in matters of insurance company administration and management. The committee so designated shall, acting through not less than a majority of its members, determine whether or not such plan of merger, consolidation, reorganization or reinsurance is practicable and desirable, having due regard to the interests of all persons interested in the New Company. If the committee determine that such plan is practical and desirable it shall determine a reasonable time which should be allowed for the consummation of the plan. Thereupon the New Company with the written approval of the Conservator or Liquidator, if then there be one, may submit to a vote of the policy holders (voting in the manner then prescribed by the laws of the State of California relating to voluntary mutualization) a proposal to suspend the mutualization provisions of this agreement for the time fixed by the com-

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mittee, which proposal shall contain a brief description of the plan. If a majority of the policy holders so voting (but not less than ten percent (10%) of those entitled to vote) vote in favor of the proposal, said provisions for mutualization shall be suspended for the time so specified and for the sole purpose of consummating the particular plan; and said plan may be consummated within said time free from said provisions and as though no such provisions had ever been contained in this agreement; but unless said plan be consummated within such time said provisions ipso facto shall become fully effective as though there had been no suspension thereof.

"The New Company shall, however, at least fifteen (15) days before any vote of policy holders is called under the provisions of this sub-paragraph, give written notice to each of its General Agents of the intention to call or take such vote. Such notice shall be deemed sufficiently given if and when it is deposited in the United States mails in a properly stamped container, addressed to such General Agent at his latest address appearing on the records of the New Company.

"(c) At any time while the stock of the New Company is held by the Conservator or the Liquidator and has not been sold by him the Old company shall have the right to pay to the Conservator or to the Liquidator the full amount then required by the New Company to complete the restoration of Non-Can benefits and also the amount required by the Conservator or Liquidator to complete the payment of all his claims and liabilities. In the event the benefits on Non-Can Policies shall have been fully restored from earnings of the New Company, contributions of the Old Company, or its shareholders, or otherwise, and all expenses of and claims against the Conservator or Liquidator of the Old Company have been fully paid, the Conservator or such Liquidator shall, upon order of the Court, distribute the stock then held by him in the manner provided by law; provided, however, that if such distribution is made prior to the expiration of the option to mutualize granted in sub-paragraph (a) of this paragraph 20, the distributees

and their successors in the ownership of said stock, shall remain bound, until the expiration of said option, to the aforesaid consent to any mutualization plan of the New Company proposed in accordance with the provisions of sub-paragraph (a) of this paragraph 20.

"The Conservator or Liquidator shall cause to be endorsed upon the certificates evidencing the ownership of such stock an appropriate legend giving notice of the said option to mutualize; and the New Company shall cause a similar legend to be endorsed upon all certificates into which the same may be transferred prior to the expiration of said option.

"(d) In the event the Conservator or Liquidator shall at any time determine that conditions are such as to require a sale of said stock, or any thereof, for the protection of the estate in conservation or liquidation, the New Company, or its policy holders, he may sell the same upon order of the Court made after a proper showing of the necessity for such sale upon a full hearing, of which hearing notice shall be given to such parties as the Court may determine are interested therein, and in such manner as the Court may direct.

"(e) It is the purpose, spirit, and intent of this agreement that, unless the provisions for mutualization are eliminated pursuant to the provisions of subparagraph (b) of this paragraph 20, the stock of the New Company shall not be sold or disposed of prior to the full restoration of benefits under Non-Can Policies except by proceedings for mutualization, so long as a reasonable probability of completing restoration of benefits under Non-Can Policies shall continue; and also, to the end that benefits under Non-Can Policies may be restored as early as practicable, the New Company declares that it will be its policy, at all times while its stock is held by the Conservator or Liquidator, so far as is reasonably practicable in the ordinary and reasonable conduct of its business, to endeavor to write new Non-Participating insurance in an amount equal to or in excess of the amount of new Participating Insurance written by it.

"(f) If the provisions of this paragraph 20, or of any one or more of the subparagraphs hereof, should be contrary to law or illegal or void, then such paragraph, subparagraph, or subparagraphs, shall be null and void, and shall be deemed separable from the remaining covenants and agreements in this agreement contained; and shall in no way affect the validity of any of the remaining provisions of this agreement."

"PLAN FOR VOLUNTARY MUTUALIZATION OF PACIFIC MUTUAL LIFE INSURANCE COMPANY

"This Plan for voluntary mutualization of Pacific Mutual Life Insurance Company has been formulated by the Pacific Mutual Price Determination Committee under the authority and in accordance with the provisions of paragraph 20 (a) of the Rehabilitation and Reinsurance Agreement entered into as of July 22, 1936, by and between Pacific Mutual Life Insurance Company and Samuel L. Carpenter, Jr., as Insurance Commissioner of the State of California, and as Conservator of The Pacific Mutual Life Insurance Company of California. The general purpose of this Plan is to determine the price for which and to prescribe the procedure by which Pacific Mutual Life Insurance Company, if said Plan is duly approved and adopted, shall purchase and cancel all the outstanding shares of its capital stock and be converted from a stock corporation into a nonstock mutual life and disability insurance corporation conducted for the benefit of its members who shall be the policy holders of the Participating and Non-Participating Life classes.

"The beneficial interest in said outstanding shares of stock is presently reserved to the Insurance Commissioner of the State of California as Liquidator of the Old Company. The liability of the Old Company under the Non-Cancellable Accident and Health insurance policies issued by it was reinsured and assumed by Pacific Mutual Life Insurance Company at the varying percentages of their stated benefits and under the terms and conditions set forth in paragraphs 10 and 11 of said Rehabilitation and Reinsurance Agreement.

"Certain words and phrases as used in this Plan have the following meaning:

"Pacific Mutual Life Insurance Company is a California corporation authorized to transact and transacting the business of life insurance and disability insurance in California and elsewhere. It is hereinafter sometimes referred to as "the Corporation."

"The Pacific Mutual Life Insurance Company of California is a California corporation, now in liquidation, and the predecessor in the transaction of insurance business of Pacific Mutual Life Insurance Company. It is herein and hereinafter sometimes referred to as "Old Company."

"The Insurance Commissioner of the State of California became the Conservator of the Old Company by virtue of an order made and entered by the Superior Court of the State of California in and for the County of Los Angeles on August 11, 1936. Said Insurance Commissioner became the Liquidator of the Old Company by virtue of an order made and entered by said Superior Court on February 3, 1937. He, or his successor in office from time to time, is hereinafter referred to as the Insurance Commissioner, Conservator or Liquidator, respectively.

"Wherever the term "Non-Cancellable Accident and Health insurance policies" or similar term is used herein, it refers to the "Non-Can Policies" as defined in said Rehabilitation and Reinsurance Agreement.

" 'Restoration of Non-Cancellable Accident and Health benefits' (sometimes hereinafter referred to simply as "restoration") means full restoration of said benefits, including deferred restoration balances, with interest, as provided in paragraph 14 of said Rehabilitation and Reinsurance Agreement.

I

Purchase Price

"A. The price to be paid by the Corporation for said outstanding shares is three million dollars ($3,000,000) with interest and subject to further augmentation as here-

inafter provided, all to be paid in one sum (unless divided to comply with the possibility provided for in Section VII hereof). In the event that restoration of said Non-Cancellable Accident and Health benefits is accomplished prior to January 1, 1973, said sum of three million dollars ($3,000,000) shall be increased by an additional sum of two hundred fifty thousand dollars ($250,000) for each full calendar year by which the date of completion of restoration antedates December 31, 1973.

"B. Said sum of three million dollars ($3,000,000) shall bear simple interest from December 31, 1948, until paid. Any additional sum added to said price if and by virtue of the fact that restoration is completed before January 1, 1973, shall bear simple interest from the date of completion of restoration until payment of the purchase price. The rate of all such interest shall be in each calendar year the stated interest rate (i.e., the interest rate stated on the face of the instrument or coupon attached thereto) of the furthest maturity United States Government bonds, publicly held and quoted and having a stated interest rate, which were outstanding at the end of the preceding calendar year, as determined for this purpose by the Treasurer of the Corporation.

II

Source of Payment and Provisos With Relation Thereto

"A. For the purpose of accumulating a fund to be used in payment, at least in part, of the purchase price, including interest, computed as above stated, for said shares, the board of directors of the Corporation shall, as soon as practicable after the close of each calendar year beginning with the year 1949, cause to be set aside in a Special Surplus Fund created for this purpose five per cent (5%) of the net profits of the Participating Department for such year, excluding, however, that part of the net profits allocable to contracts reinsured under said Rehabilitation and Reinsurance Agreement. Net profits for this purpose are net profits from whatever source (not thus excluded), before dividends, but after charging thereto the cost of acquisition

of new Participating business, and after taking into consideration taxes, gains or losses on the sale or other disposition of assets, and such reasonable adjustment in the value of any assets, or reserves for anticipated losses thereon, or otherwise, as the board of directors of the Corporation may from time to time establish, and after deducting therefrom the amount of interest which is added for that year to the Special Surplus Fund, as provided in paragraph B of this Section. Credits from profits into this Special Surplus Fund shall continue until the purchase price for said shares, with interest as specified, has been paid in accordance with Section IV of this Plan, subject to the qualification that the Fund at no time shall exceed the then maximum purchase price as provided herein including interest, less the amount of the capital of the Corporation, and any such excess shall be credited back to the general surplus of the Participating Department.

"B. Simple interest equal to the stated interest rate of the furthest maturity United States Government bonds, publicly held and quoted, which were outstanding at the close of the preceding calendar year, as determined for this purpose by the Treasurer of the Corporation, shall each year be added to said Special Surplus Fund from the net profits of the Participating Department and shall be accounted for as a part of said Fund.

"C. Said Special Surplus Fund shall be considered and treated as part of the surplus of the Participating Department but may not be distributed or disbursed except as provided in this Plan, or as needed to pay policy obligations (other than dividends) of the Participating Department. No allocation of the net profits of the Participating Department shall be made to said Special Surplus Fund other than as above provided, it being intended herein that said annual interest on the sum standing in said Fund be considered the only earnings of said Fund.

"D. The price of the shares with interest as defined herein shall be paid when and if all of the following conditions have been met, and not until then:

1. Restoration is completed.

2. The funds standing in said Special Surplus Fund, plus the capital and surplus standing in the general corporate accounts, equal or exceed the price of the shares with interest as specified herein.

3. The financial condition of the Corporation is such that after paying for and cancelling the shares it would still have admitted assets in excess of all its liabilities (both valued on bases held to be satisfactory by a majority of the Voting Trustees appointed and acting pursuant to Section III of this Plan, whose decision shall be final and binding on all interested parties) to the amount of the sum of (a) and (b) as follows: (a) four per cent (4%) of all its admitted assets according to the form of annual statement required for life insurance companies by the State of California, if any, or in the absence of such requirement, according to the form of annual statement then in general use, plus (b) twenty-five per cent (25%) of the premiums collected during the preceding calendar year on all Group insurance written on the one-year term basis and on all Accident and Health insurance.

"E. The excess of the amount paid for the shares over the amount of the capital of the Corporation shall be charged against the Special Surplus Fund and the general corporate surplus in the respective proportions which exist at the time of payment between the Special Surplus Fund on the one hand and the general corporate surplus on the other. Any amounts remaining in the Special Surplus Fund after the price of the shares has been paid and so allocated, shall revert to the general surplus of the Participating Department for the benefit of the remaining and continuing members of the class of participating life policies which contributed to the Special Surplus Fund, and the surplus applicable to such class of policy holders shall be entitled to credits from time to time in the discretion of the board of directors from corporate surplus or sources contributing thereto, until there shall have been recovered to it a total sum equal to that part of the price of the shares

which was allocated against the Special Surplus Fund, with simple interest thereon from the date of payment for the shares at rates of interest determined from year to year in the manner set forth in paragraph B of Section I of this Plan.

"F. Neither the accumulation of said Special Surplus Fund, nor any other provision of this Mutualization Plan, shall affect the provisions of paragraph 17 or of paragraph 14 of said Rehabilitation and Reinsurance Agreement or the right of the holders of Non-Cancellable Accident and Health policies to the restoration of benefits thereunder from the sources and in the manner therein provided.

III

"Voting Trust

"A. Legal title to said outstanding shares of stock of the Corporation is presently held by Victor H. Rosetti, Harvey S. Mudd, Rufus B. Von Kleinsmid, Colbert Coldwell, A Crawford Greene, Silas H. Palmer and Wallace K. Downey, as Voting Trustees under the authority of the Pacific Mutual Voting Trust Agreement dated April 4, 1938, entered into by and between said Voting Trustees or their predecessors in interest, and by Samuel L. Carpenter, Jr., as Conservator or Liquidator of The Pacific Mutual Life Insurance Company of California and as "Depositor" under said Pacific Mutual Voting Trust Agreement, and by Pacific Mutual Life Insurance Company. The Insurance Commissioner of the State of California as Liquidator of The Pacific Mutual Life Insurance Company of California is the owner of the beneficial interest in said shares. By its terms said Pacific Mutual Voting Trust Agreement of April 4, 1938, shall immediately terminate upon the adoption of any plan for the mutualization of the Corporation, except as to the extent such plan may otherwise provide. The certificates representing said shares of stock have been issued in or transferred to the names of said trustees under said Pacific Mutual Voting Trust Agreement and show thereon that they were issued pursuant to that said Agreement and such fact is also

indicated on the books of the Corporation. Upon the effective date of this Plan, therefore, the Voting Trust set up in said Pacific Mutual Voting Trust Agreement of April 4, 1938, shall immediately terminate and end. The said shares of stock, upon being distributed to the Conservator or Liquidator as provided in said Pacific Mutual Voting Trust Agreement of April 4, 1938, shall be immediately disposed of by said Conservator or Liquidator by transfer to the Voting Trustees of the new Voting Trust hereinafter provided and established, and the certificates therefor shall show that said shares are held pursuant to said new Voting Trust Agreement and such fact shall also be noted on the books of the Corporation. From that time on, all of said shares of stock shall be held and disposed of by said Voting Trustees, or their successors, upon the terms and conditions of said New Voting Trust Agreement.

"B. During the period while this Plan is in effect and pending the payment of said purchase price, a Voting Trust of said shares shall be established and maintained in the form appended hereto as hereinafter in this Section set forth. The following individuals are designated as initial Voting Trustees:

Victor H. Rossetti
Harvey S. Mudd
Rufus B. Von Kleinsmid
Colbert Coldwell
A. Crawford Greene
Silas H. Palmer
Allard A. Calkins
Herbert Hoover, Jr.
Wallace K. Downey

"Wallace K. Downey is named herein because he is now the Insurance Commissioner of the State of California, but if, as, and when his successor becomes such Insurance Commissioner such successor shall become the Voting Trustee under this Plan as initial Voting Trustee or otherwise in place of the said Wallace K. Downey.

"Said new Voting Trust Agreement shall be in the form appended to and made a part of this Plan, and marked

"APPENDIX—FORM OF NEW VOTING TRUST AGREEMENT."

"C. If by reason of any provision of law or otherwise said Voting Trust should fail or be terminated contrary to its terms, such failure or termination shall not adversely affect the balance of this Plan, but in such event said shares shall be returned to the Depositor who shall hold, use, and exercise all of the rights of owner thereof and dispose of such shares, all subject to said Rehabilitation and Reinsurance Agreement and in accordance with said Plan; provided that he shall in such event, if and to the extent that it shall be lawful, create a new Voting Trust with the same Voting Trustees and upon such of the terms hereinabove provided as may be legally permissible and shall transfer said shares to said Voting Trustees to hold and dispose of said shares in accordance therewith.

"If at any time before completion or failure of the mutualization as herein provided, the Voting Trust provided in this Section III shall fail or terminate so as to leave no Voting Trustees acting and qualified for the performance of the powers and duties conferred upon them hereunder, and if the Insurance Commissioner is prevented by any provision of law from establishing a voting trust to take the place of the Voting Trust established by this Plan, the Insurance Commissioner shall himself perform the functions and duties of the Voting Trustees as set forth herein, and particularly, without limiting the generality of the foregoing, their functions and duties enumerated in paragraph D of this Section III and in paragraph D of Section II.

"D. It is the policy of the Corporation, as declared in paragraph 20(e) of said Rehabilitation Agreement, in so far as reasonably practicable in the ordinary course of business and for so long as such policy may be anticipated to have the effect of accelerating restoration, to write at least one half of its new life insurance, other than Group insurance, each year as Non-Participating insurance. In the event that, prior to restoration of said benefits to the extent of ninety per cent (90%) of the difference between the full benefit amount and the amount originally assumed,

the Corporation in each of three (3) successive calendar years does not write at least forty per cent (40%) in face amount (or, if there is no face amount, in commuted value) of its new life insurance, other than Group insurance, as Non-Participating insurance, the Trustees shall appoint from the directors of the Corporation a Committee of not less than three (3) nor more than five (5) members who shall as promptly as possible make a study and written report thereon to the Trustees showing (1) the effect of such departure from the declared policy upon (a) the progress toward completion of restoration, (b) the ultimate price for the shares and time of payment of the same, and (c) the general good of the Corporation, and (2) the justification for such departure from the declared policy. The Trustees shall then decide whether in the circumstances such justification existed, and if not, what action, if any, they should take at the next election of directors.

IV

"Effectuation of Mutualization

(Payment for Shares; Surrender and Cancellation of Certificates; Amendment of Articles of Incorporation)

"A. When, as, and if, after restoration, the financial condition of the Corporation shall permit making payment for said shares in accordance with the provisions of paragraph D of Section II hereof, and the other conditions set forth in the Plan, precedent to the payment of the purchase price, shall have been met and fulfilled, the Corporation shall thereupon become obligated to purchase said shares, and the board of directors shall authorize and direct the Treasurer of the Corporation to pay to the order of the Insurance Commissioner of the State of California, as Liquidator of The Pacific Mutual Life Insurance Company of California, the price for said shares, including interest, as specified in Section I of this Plan. The board of directors shall cause the Articles of Incorporation to be duly amended in the following particulars: Articles Four, Five and Seven as they now read, or the present substance of

them if they should have been amended, shall be deleted. The following shall be substituted for said Article Four:

> "Four: This corporation shall be a nonstock life and disability insurance corporation, conducted for the benefit of its members who shall be the policyholders of the Participating and Non-Participating Life classes."

"The following shall be substituted for said Article Seven:

> "Seven: This corporation expressly reserves the right to amend its articles of incorporation from time to time in such manner and for such purposes as may at the time be permitted by law."

"B. Upon receipt of the payment referred to in paragraph A of this Section, the Liquidator shall notify the Trustees under the Voting Trust established under Section III of this Plan (being also the Trustees under any second voting trust created under Section VII hereof) of the fact of such payment, and said Trustees shall promptly vote for or consent in writing to the amendments of the Articles of Incorporation of the Corporation referred to in said paragraph A, and thereupon shall deliver to the Liquidator the certificates for the said shares of stock duly endorsed. The Liquidator shall thereupon endorse said certificates and surrender them to the Treasurer of the Corporation, who shall cause them to be cancelled.

"C. When all of said outstanding shares have been acquired and cancelled, and the certificate of amendment of the Articles of Incorporation has been duly filed as provided by law, this Plan shall be deemed to be completed and shall terminate, and the Corporation shall be and thenceforth become a nonstock life and disability insurance corporation conducted for the benefit of its members, as provided by law, with due account taken of the right of recovery to the surplus of the Participating Department provided in paragraph E of Section II above.

V

"Approval of Plan

"A. By the terms of paragraph 20(a) of said Rehabilitation and Reinsurance Agreement, Samuel L. Carpenter, Jr., as Conservator of the Old Company, for himself and for any successors in ownership of said stock claiming under him in any manner other than through a sale of said stock pursuant to the provisions of paragraph 20(d) of said Agreement, thereby consented to this Plan of Mutualization and agreed to dispose of said stock in the manner herein provided.

"B. This Plan shall become effective upon being filed in the office of the Insurance Commissioner of the State of California after having been adopted and approved as provided by law, and the date of such filing shall be the effective date of the Plan. The Corporation shall thereupon be obligated to proceed in accordance with the Plan to purchase said shares if, as, and when the financial condition of the Corporation shall permit the making of the payment for said shares in accordance with the provisions of paragraph D of Section II hereof, and the other conditions precedent to the payment of the purchase price for said shares set forth in the Plan have been met and fulfilled.

"C. Within sixty (60) days after the making of the Report of the Price Determination Committee, the Corporation, pursuant to paragraph 20(a) of said Rehabilitation Agreement, shall mail copies of said Report to all of its policyholders entitled by law to vote upon this Plan. The Corporation may at the same time mail to each such policyholder such notice, explanatory statement, and form of policyholder's request for submission of the Plan, as in the opinion of the management of the Corporation may be appropriate to facilitate the procedure provided in said paragraph 20(a) of said Rehabilitation Agreement. If within one hundred twenty (120) days after the mailing of such notice, ten per cent (10%) of such policyholders entitled to vote upon any such Plan (each policyholder being for this purpose regarded as one person regardless of the number of policies owned or amount of insurance held)

shall request in writing the submission thereof, the Corporation shall promptly submit the same in accordance with the laws of the State of California then in effect.

"D. The election by the policyholders eligible to vote upon the Plan shall be called by the board of directors of the Corporation, who shall set the date for such election and cause notice thereof to be mailed to the policyholders entitled to vote from the principal office of the Corporation at least thirty (30) days prior to the date set for such election, as provided by law. Voting shall be by mail upon ballots in the following form, completed as appropriate:

"BALLOT ON PLAN OF MUTUALIZATION OF PACIFIC MUTUAL LIFE INSURANCE COMPANY

The undersigned holder of a policy or policies of Participating or Non-Participating Life Insurance in Pacific Mutual Life Insurance Company hereby acknowledges receipt of a copy of the report of the Pacific Mutual Price Determination Committee, dated ..... 19....., which report included a copy of the Plan of Mutualization of said Pacific Mutual Life Insurance Company.

The undersigned votes on the approval of the above-referred to Plan of Mutualization as indicated below:

	FOR	AGAINST
Approval of the Plan of Mutualization of Pacific Mutual Life Insurance Company contained in the report of the Pacific Mutual Price Determination Committee dated.....	☐	☐

Signature.....

Dated: .....,"

The ballot form may also include a policy number and any other appropriate identifying data. A form of such ballot shall be mailed with the notice of election. If ballots from at least five per cent (5%) of the policyholders entitled to vote at such election shall not have been received at the

principal office of the Corporation by 12 o'clock noon, Pacific Standard Time, of the date set for such election, the board of directors of the Corporation may extend the time for receiving ballots for a period not exceeding thirty (30) days from the date set for such election; and the notice of the election shall so state. The Corporation may mail to the eligible policyholders, together with the notice of the election and form of ballot, any such copy or copies of the Report of the Price Determination Committee, Plan of Mutualization, explanatory statement, statement or certificate of the Insurance Commissioner of the State of California relative to the Plan, return envelope or other matter as may in the opinion of the management of the Corporation be appropriate for the information of the policyholders or to facilitate such election. The inspectors of election who shall be appointed pursuant to and who shall perform the functions and duties prescribed by section 11528 of the Insurance Code of the State of California shall designate one of their number to act as chairman, and any vacancy among said inspectors of election occurring during the canvass of the mail vote may be filled by such chairman. The Corporation shall furnish the inspectors of election with such facilities, equipment and personnel as they may require for the performance of their duties.

VI

"Failure of Consummation of Mutualization

"In the event that the price of said shares shall not have been paid, as herein provided, by December 31, 1983, this Mutualization Plan shall be considered to have failed, the Voting Trust established pursuant to Section III hereof shall terminate and said shares of stock shall be returned to the Liquidator as therein provided, and any amounts then standing in said Special Surplus Fund shall revert to the general surplus of the Participating Department of the Corporation.

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VII

"Second Voting Trust

"This Plan contemplates that the purchase of all of the shares shall be consummated at one time and does not contemplate any interim or piecemeal purchase of less than all of the shares. If, however, at any time it should become necessary or requisite for the effectuation or validity of this Plan or of the Voting Trust created under Section III hereof, that there be a second voting trust created under the provisions of section 11529 of the Insurance Code of the State of California, such second voting trust shall be created in accordance with the provisions of that section and the terms of said second voting trust shall otherwise be as nearly as possible identical with the terms of the Voting Trust created under Section III hereof, and the Corporation shall appoint as the initial trustees thereof, subject to the approval of the Insurance Commissioner, the persons who are then the Trustees under the Voting Trust created under Section III hereof and any person who thereafter ceases to be a Trustee under the Voting Trust created under said Section III shall cease to be a trustee under the second voting trust, and any person who is appointed a Trustee under the Voting Trust created under said Section III shall be appointed a successor trustee under the second voting trust; and if it should further become necessary or requisite for the effectuation or validity of this Plan or of the Voting Trust created under Section III hereof, then consistent with the purposes and general terms of this Plan and after restoration is completed, the Corporation may purchase not less than ninety-nine per cent (99%) of said shares at a price consistent with the price for the shares which is provided in the Plan and subject to all the restrictions which are set forth in Section II, paragraph D, of this Plan, and such shares, together with the voting rights thereof, shall thereupon be transferred to the trustees of such second voting trust, and the remaining shares shall thereafter be purchased and similarly transferred together with the voting rights thereof as promptly as possible in accordance with the Plan. This Section is

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included in the Plan solely for the purpose of insuring full compliance with section 11529 of the Insurance Code of the State of California and for no other purpose, and shall not be effective unless required for that purpose.

VIII

"INTERPRETATION OF PLAN

"This Plan shall be deemed to incorporate all provisions required by law or by said Rehabilitation Agreement to be incorporated herein. The Plan is intended to comply strictly with all applicable provisions of law and of said Rehabilitation Agreement and shall be so interpreted."

APPENDIX E

Judgment Appealed From

"IN THE
SUPREME COURT OF THE STATE OF CALIFORNIA

L.A. No. 23261

THE PACIFIC MUTUAL LIFE INSURANCE COMPANY OF CALIFORNIA, ET AL., *Appellants*

VS.

F. BRITTON MCCONNELL, as Insurance Commissioner, etc., et al., *Respondents*

On Appeal From the Superior Court in and For the County of Los Angeles

Superior Court No. 579832

The above entitled cause having been heretofore argued, and submitted and taken under advisement, and all and singular the law and premises having been fully considered,

IT IS ORDERED, ADJUDGED AND DECREED by the Court that the

JUDGMENT

of the Superior Court in and for the County of Los Angeles in the above entitled cause be and the same is hereby affirmed.

Respondents to recover costs on appeal."

I, William I. Sullivan, Clerk of the Supreme Court of California, do hereby certify that the foregoing is a true copy of an original judgment entered in the above entitled cause on the 27th day of June, 1955, and now remaining of record in my office.

WITNESS my hand and the seal of the Court, affixed at my office, this 1st day of August, A.D. 1955.

WILLIAM I. SULLIVAN,
Clerk.
By PAUL DINOIA
Deputy

APPENDIX F

STATUTES

1. Insurance Code of California

§ 11525. AUTHORIZATION TO MUTUALIZE. A solvent domestic incorporated insurer having a paid-in capital represented by outstanding shares of capital stock and issuing, on a reserve basis, nonassessable policies of life insurance or of both life and disability insurance, may convert itself into an incorporated mutual life insurer, or life and disability insurer, issuing nonassessable policies on a reserve basis. To that end it may provide and carry out a plan for the acquisition of the outstanding shares of its capital stock for the benefit of its policyholders, or any class or classes of its policyholders, by complying with the requirements of this chapter.

§ 11526. METHOD OF MUTUALIZATION. Such plan shall include appropriate proceedings for amending the insurer's articles of incorporation to give effect to the acquisition, by said insurer, for the benefit of its policyholders or any class or classes thereof, of the outstanding shares of its capital stock and the conversion of the insurer from a stock corporation into a nonstock corporation for the benefit of its members. The members of such nonstock corporation shall be the policyholders from time to time of the class or classes for whose benefit the stock of the insurer was acquired, and no other persons. Such plan shall be:

(a) Adopted by a vote of a majority of the directors.

(b) Approved by the vote of the holders of at least a majority of the outstanding shares at a special meeting of shareholders called for that purpose, or by the written consent of such shareholders.

(c) Submitted to the commissioner and approved by him in writing.

(d) Approved by a majority vote of all the policyholders of the class or classes for whose benefit the stock is to be acquired voting at an election by the policyholders called for

that purpose, subject to the provisions of Section 11528. The terms "policyholder" and "policyholders" as used in this chapter shall be deemed to mean the person or persons insured under an individual policy of life insurance, or of disability insurance, or of any combination of life and disability insurance. They shall also include the person or persons to whom any annuity or pure endowment is presently or prospectively payable by the terms of an individual annuity or pure endowment contract, except where the policy or contract declares some other person to be the owner or holder thereof, in which case such other person shall be deemed the policyholder. In any case where such policy or contract names two or more persons as joint insureds, payees, owners or holders thereof, the persons so named shall be deemed collectively to be but one policyholder for the purpose of this chapter. In any case where a policy or contract shall have been assigned by assignment absolute on its face to an assignee other than the insurer, and such assignment shall have been filed at the principal office of the insurer at least 30 days prior to the date of any election or meeting referred to in this chapter, then such assignee shall be deemed at such election or meeting to be the policyholder. For the purpose of this chapter the terms "policyholder" and "policyholders" include the employer to whom, or a president, secretary or other executive officer of any corporation or association to which a master group policy has been issued, but exclude the holders of certificates or policies issued under or in connection with a master group policy. Beneficiaries under unmatured contracts shall not as such be deemed to be policyholders.

(e) Filed in the office of the Insurance Commissioner after having been approved as provided in subdivisions (b), (c) and (d) of this section.

§ 11527. EXAMINATION OF PLAN BY COMMISSIONER: CONDITIONS PREREQUISITE TO APPROVAL. The commissioner shall examine the plan submitted to him under the provisions of subdivision (c) of section 11526. He shall not approve such plan unless in his opinion the rights and interests of the insurer, its policyholders and shareholders are protected

nor unless he is satisfied that the plan will be fair and equitable in its operation.

* * * * * * * * * *

§ 11528. APPROVAL BY POLICYHOLDERS.

[*Calling election: Policyholder to have one vote: Notice of election.*] The election prescribed by subdivision (d) of section 11526, shall be called by the board of directors or the president and every policyholder of the class or classes for whose benefit the stock is to be acquired, whose insurance shall have been in force for at least one year prior to such election shall have one vote, regardless of the number of policies or amount of insurance he holds, and regardless of whether such policies are policies of life insurance or policies of disability insurance. Notice of such election shall be given to policyholders entitled to vote by mail from the principal office of such insurer at least thirty days prior to the date set for such election, in a sealed envelope, postage prepaid, addressed to each such policyholder at his last known address.

[*Voting methods.*] Voting shall be by one of the following methods:

(a) At a meeting of such policyholders, held pursuant to such notice, by ballot in person or by proxy.

(b) If not by the method described in subdivision (a) of this section, then by mail pursuant to a procedure and on forms to be prescribed by such plan.

[*Conduct of election.*] Such election shall be conducted under the direction and supervision of three impartial and disinterested inspectors appointed by the insurer and approved by the commissioner. In case any person appointed as inspector fails to appear at such meeting or fails or refused [refuses] to act at such election, the vacancy, if occurring in advance of the convening of the meeting or in advance of the opening of the mail vote, may be filled in the manner prescribed for the appointment of inspectors and, if occurring at the meeting or during the canvass of the mail vote, may be filled by the person acting as chairman of said meeting or designated for that purpose in such

plan. The decision, act or certificate of a majority of the inspectors shall be effective in all respects as the decision, act or certificate of all. The inspectors of election shall determine the number of policyholders, the voting power of each, the policyholders represented at the meeting or voting by mail, the existence of a quorum and the authenticity, validity and effect of proxies. They shall receive votes, hear and determine all challenges and questions in any way arising in connection with the right to vote, count and tabulate all votes, determine the result, and do such other acts as are proper to conduct the vote with fairness to all policyholders. The inspectors of election shall, before commencing performance of their duties, subscribe to and file with the insurer and with the commissioner an oath that they, and each of them, will perform their duties impartially, in good faith, to the best of their ability and as expeditiously as is practicable. On the request of the insurer, the commissioner, a policyholder or his proxy, the inspectors shall make a report in writing of any challenge or question or matter determined by them and execute a certificate of any fact found by them. They shall also certify the result of such vote to the insurer and to the commissioner. Any report or certificate made by them shall be prima facie evidence of facts stated therein. All necessary expenses incurred in connection with such election shall be paid by the insurer. For the purpose of this section, a quorum shall consist of five per centum of the policyholders of such insurer entitled to vote at such election.

§ 11529. ACQUISITION OF STOCK: ASSIGNMENT IN TRUST: VOTING STOCK: CANCELLATION OF SHARES: EFFECT: TERMINATION OF VOTING TRUST: DISPOSITION OF SHARES. In carrying out any such plan, the insurer may acquire any shares of its own stock by gift, bequest or purchase. Any shares so acquired shall, unless as a result of such acquisition all of the shares of the insurer shall have been acquired, be acquired in trust for the policyholders of the class or classes for whose benefit the plan provides that the stock of the insurer shall be acquired as hereinafter provided. Such shares shall be assigned and transferred on the books of such insurer to three or more trustees appointed by the in-

surer and approved by the commissioner under a trust agreement approved by the commissioner. Such trustees shall hold such stock in trust until all of the outstanding shares of capital stock of such insurer have been acquired, but for not longer than 30 years with such extensions of not more more than five years each as may be granted by the commissioner. Such extensions may be granted by the commissioner if the plan so provides and if in his opinion the plan of acquisition of all of such stock can be completed within a reasonable period. Such trustees shall vote such stock at all corporate meetings at which stockholders have the right to vote. When all of the outstanding shares of capital stock of such insurer have been acquired, all said shares shall be canceled, the certificate of amendment of the insurer's articles of incorporation giving effect thereto shall be filed in accordance with the provisions of Section 362b of the Civil Code, and the insurer shall become a nonstock corporation for the profit of its members and such trust shall thereupon terminate. Thereafter such corporation shall be conducted for the mutual benefit, ratably, of its policyholders of the class or classes for whose benefit the stock was acquired and shall, upon issuance to it by the commissioner of a certificate of authority, have power to issue nonassessable policies on a reserve basis subject to all provisions of law applicable to incorporated life insurers or life and disability insurers, as the case may be, issuing nonassessable policies on a reserve basis, but shall be exempt from the provisions of Chapter 7 of Part 2 of Division 2 of this code. Policies so issued may be upon the basis of full or partial participation therein as agreed between the insurer and the insured.

Upon the termination of any such voting trust, either in accordance with its term or as hereinabove provided, such plan of mutualization shall terminate, unless theretofore completed. Upon such termination, unless the plan of mutualization provides for the disposition of the shares acquired by the insurer under such plan or for the disposition of the proceeds thereof, the shares held by such trustees shall be disposed of in accordance with an order of the superior court of the county in which is located the princi-

pal office of such insurer, made upon a verified application of the commissioner.

§ 11529.5. VOTING TRUST: CREATION: NAMING TRUSTEES: APPROVAL OF COMMISSIONER: TRANSFER OF SHARES TO TRUSTEES: IRREVOCABILITY OF TRUST: TERMINATION. Any such plan of mutualization may provide for the creation of a voting trust under a trust agreement for the holding and voting by three or more trustees of any portion or all of the shares of the insurer not acquired upon the adoption of such plan. The voting trustees shall be named in accordance with such plan or, if no provision is made therein for the naming of such trustees, then by the insurer. The voting trust agreement and voting trustees shall be subject to the approval of the commissioner. Any or all of the trustees under such voting trust agreement may be the same person or persons as any or all of the trustees referred to in Section 11529. Such voting trust agreement shall provide that in the event of acquisition by the insurer of any of the shares of stock held thereunder in accordance with the provisions of the plan, such shares so acquired together with the voting rights thereof shall be transferred by the trustees named under the provisions of this section to the trustees named under the provisions of Section 11529. Any voting trust agreement created pursuant to the provisions of this section may be made irrevocable for not longer than thirty (30) years and thereafter until the termination of the trust provided for in Section 11529. The trust created pursuant to the provisions of this section shall terminate in any event upon termination of the trust provided for in Section 11529. Upon the termination of the trust created pursuant to the provision of this section, any shares held in such trust shall revert to the persons entitled thereto by law.

§ 11530. PAYMENT FOR STOCK: APPROVAL BY COMMISSIONER: CONDITIONS. Every payment for the acquisition of any share of the capital stock of such insurer, the purchase price of which is not fixed by such plan, shall be subject to the prior approval of the commissioner. Neither such plan, nor any such payment, may be approved by the commissioner unless he finds that the rights and interests of

the insurer, its policyholders, and shareholders are protected.

§ 11531. FILING ACCEPTANCE OF APPOINTMENTS BY TRUSTEES: REPAYMENT OF DIVIDENDS TO INSURER. The trustees referred to in section 11529 shall file with such insurer and with the commissioner a verified acceptance of their appointments and verified declarations that they will faithfully discharge their duties as such trustees. All dividends and other sums received by said trustees on the shares held by them, after paying the necessary expenses of executing their trust, shall be immediately repaid to such insurer for the benefit of all who are, or may become, policyholders of such insurer of the class or classes for whose benefit the stock of such insurer was acquired and entitled to participate in the profits thereof and shall be added to and become a part of the assets of such insurer.

§ 11532. MUTUALIZED INSURER TO BE CONTINATION OF ORIGINAL INSURER: EFFECT OF MUTUALIZATION: RIGHTS, POWERS AND DUTIES AFTER MUTUALIZATION. Such insurer, after mutualization, shall be a continuation of the original insurer, and such mutualization shall not affect existing suits, rights or contracts except as provided in said plan for the acquisition of the outstanding shares of the capital stock of such insurer, approved as provided in this chapter. Such insurer, after mutualization, shall exercise all the rights and powers and perform all the duties conferred or imposed by law upon insurers writing the classes of insurance written by it, and to protect rights and contracts existing prior to mutualization, subject to the effect of said plan.

§ 11532.1. MEETINGS: ANNUAL MEETING. An annual meeting of members shall be held at 10 o'clock in the morning of the fourth Tuesday of March of each year at the principal office of the insurer, unless a different time or place be provided in the by-laws.

§ 11532.2. SAME: SPECIAL MEETINGS. Special meetings of the members, for any purpose or purposes whatsoever, may be called at any time by the president, or by the board of directors, or by one or more members holding not less than

one-fifth of the voting power of such insurer, or by such other officers or persons as the by-laws authorize.

§ 11532.3. SAME: NOTICE OF MEETINGS: HOW GIVEN: CONTENTS. Notice of all meetings of members whether annual or special shall be given in writing to the members entitled to vote by the secretary, or an assistant secretary, or other person charged with that duty, or if there be no such officer, or in case of his neglect or refusal, by any director or member.

A notice may be given by such insurer to any member either personally, or by mail, or other means of written communication, charges prepaid, addressed to such member at his address appearing on the books of the insurer, or given by him to the insurer for the purpose of notice. If a member gives no address, notice shall be deemed to have been given him if sent by mail or other means of written communication addressed to the place where the principal office of the insurer is situated, or if published at least once in some newspaper of general circulation in the county in which said office is located.

Notice of any meeting of members shall be sent to each member thereto not less than seven days before such meeting, unless the by-laws provide otherwise.

Notice of any meeting of members shall specify the place, the day, and the hour of the meeting and the general nature of the business to be transacted.

§ 11532.4. SAME: QUORUM. The presence in person or by proxy of 5 per cent of the members entitled to vote at any meeting shall constitute a quorum for the transaction of business, unless otherwise provided in the by-laws.

§ 11532.5. SAME: MANNER OF VOTING. Each such member shall have one vote at any meeting of members regardless of the number of policies or the amount of insurance that such member holds and regardless of whether such policies are policies of life insurance, or of disability insurance, or both. Any member entitled to vote shall have the right to do so either in person or by an agent or agents authorized

by a written proxy executed by such person or his duly authorized agent and filed with the secretary of such insurer.

§ 11532.6. DIRECTORS: CONTINUANCE IN OFFICE: ELECTION. The directors of the insurer in office at the time the insurer is mutualized as provided in this chapter shall continue in office until the first annual meeting of members. At the first annual meeting of members and at each annual meeting thereafter directors shall be elected by the members for the term or terms authorized by this chapter.

§ 11532.7. SAME: DIVISION OF DIRECTORS INTO CLASSES: TERM OF OFFICE: MEMBERSHIP, ETC., IN INSURER. The articles of incorporation or the by-laws may provide that the directors may be divided into two or more classes whose terms of office shall expire at different times, but no term shall continue longer than six years. In the absence of such provisions, each director, except members of the board of directors at the time the insurer is mutualized, shall be elected for a term of one year. All directors shall hold office for the term for which they are elected and until their successors are elected and qualified. A director may, but need not be a member or policyholder of the insurer of which he is acting as director.

§ 11532.8. LAWS APPLICABLE TO MUTUALIZED INSURERS. All insurers mutualized under the provisions of this chapter shall be subject to all other applicable provisions of this code and to the provisions of the general corporation law as provided in Section 1140 of this code.

§ 11533. PROVISIONS OF CODE NOT APPLICABLE. The provisions of Article 8 of Chapter 1 of Part 2 of Division 1 of this code shall not apply to any of the following:

(a) Shares of the capital stock of such insurer acquired as provided in section 11529 and assigned and transferred to the trustees as is provided in said section, and the assignment and transfer of said shares as so provided.

(b) Any certificate or other instrument issued to a policyholder of such mutualized insurer conferring or evidencing membership in such mutualized insurer or conferring or evidencing such member's right to participate in the profits

or share in the assets of such mutualized insurer by virtue of his membership therein, and the issuance of such certificate or other instrument.

(c) The plan for the acquisition of the outstanding shares of the capital stock of such insurer authorized by the provisions of this chapter, the submission of said plan to the commissioner and to the policyholders of such insurer as provided in this chapter, and the approval and carrying out of said plan or any part thereof in accordance with the provisions of this chapter.

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§ 1043. MUTUALIZATION, REINSURANCE AND REHABILITATION.

[*Authority of commissioner: Serving as officer or director in company formed of assets or funds.*] In any proceeding under this article, the commissioner, as conservator or as liquidator, may, subject to the approval of said court, and subject to such liens as may be necessary mutualize or reinsure the business of such person, or enter into rehabilitation agreements. No commissioner who acts as conservator of such person or who mutualizes, merges or reinsures the business of such person or who enters into rehabilitation agreements affecting such person, and no deputy commissioner who has participated in the administration of the affairs of such person for the commissioner as conservator shall for a period of two years from and after the effective date of such mutualization, reinsurance or rehabilitation become an officer or director of, or serve as an officer or director of, or serve in any position of gain or profit in, any company formed in whole or in part of the assets or funds, or any part of the assets or funds of such mutualized, merged, reinsured or rehabilitated person.

[*Violation of provision: Punishment.*] Every person violating this provision is guilty of a public offense and shall be punished by imprisonment in the State prison not exceeding five years, or in the county jail not exceeding two years, or by a fine not exceeding five thousand dollars ($5,000), or by both such fine and imprisonment.

[*Provision against investment or reinvestment without commissioner's approval.*] Such rehabilitation or reinsurance agreements shall provide that, subsequent to the date thereof and for such period of time as the commissioner may determine, no investment or reinvestment of the assets of the person rehabilitated or reinsured shall be made without first obtaining the written approval of the commissioner.

[*Directing or assisting in investment or reinvestment without, or making in nonconformity with, Commissioner's approval: Punishment.*] Every party to such agreement, and every director, officer, agent and employee of such person, and every other person who knowingly in violation thereof directs or aids or assists in causing to be made an investment or reinvestment of any of said assets without first having obtained the written approval of the commissioner, or who makes such investment or reinvestment in nonconformity with the written approval of the commissioner then in effect authorizing such investment or reinvestment, is guilty of a public offense and shall be punished by imprisonment in the State prison not exceeding five years or in the county jail not exceeding two years, or by a fine not exceeding five thousand dollars ($5,000), or by both such fine and imprisonment.

§ 1044. SAME: MORATORIUM ON POLICY LOANS AND PAYMENT OF MONEY UPON SURRENDER OF POLICIES. In connection with a rehabilitation agreement under section 1043, which affects a life insurer, and in an agreement made for the reinsurance of the business of a life insurer under said section, there may be included in such rehabilitation or reinsurance agreement a provision for, and the commissioner shall have authority to impose and declare, a moratorium against the provisions of the life insurance policies therein involved calling for the making of loans on the security of such policies and for the payment of money upon the surrender of such policies, such moratorium to continue for such period and to such extent as may be directed by said court.

§ 1045. MUTUALIZATION OF LIFE INSURER ISSUING NONASSESSABLE POLICIES ON A RESERVE BASIS: FORMATION OF PLAN. If

at any time after the issuance of an order under section 1011 affecting a life insurer issuing nonassessable policies on a reserve basis and organized with a capital stock evidenced by shares thereof it shall appear to the commissioner that the purposes of section 1011 can be best attained by the mutualization of such life insurer, the commissioner may formulate a plan for the mutualization of such insurer.

§ 1046. SAME: MUTUALIZATION PLAN: REQUIRED PROVISIONS. Said mutualization plan shall include provisions for:

(a) [*Acquisition of capital stock.*] The acquisition by such insurer of all outstanding shares of its capital stock at a price and upon terms and conditions to be fixed as hereinafter provided.

(b) [*Retirement of capital stock.*] The retirement of said shares of stock when acquired by such insurer.

(c) [*Amendment of charter.*] The amendment of the charter of such insurer so as to enable it to transact its business as a mutual insurer issuing nonassessable policies on a reserve basis.

(d) [*Payment of claims.*] The manner in which and the time within which, after mutualization is effected, matured and maturing claims against such insurer shall be paid to the lawful holders thereof.

(e) [*Submission of plan to policyholders.*] The submission of said mutualization plan to the policyholders of such insurer under such procedure as shall be set forth in the plan or prescribed by said court, for their approval or rejection.

(f) [*Notice to shareholders.*] Notice to the shareholders of such insurer, in such manner and at such time after the approval of said mutualization plan by said policyholders, as the court may direct.

§ 1047. SAME: OPTIONAL PROVISIONS. Said mutualization plan may include provisions:

(a) [*Imposing moratorium against provisions calling for making loans, etc.*] Imposing a moratorium against the

provisions of the life insurance policies issued by such insurer and then in force calling for the making of loans on the security of such policies and for the payment of money upon the surrender of such policies, for a period and to an extent to be named in such provisions imposing such moratorium, and subject to extension, change or prior termination only upon the written approval of the commissioner.

(b) [*Imposing liens, etc.*] Imposing liens upon, or otherwise adjusting, the policies of the insurer so as to create or make available the minimum paid-in capital required of such an insurer to be admitted and such additional paid-in capital as will be reasonably sufficient to enable such insurer to carry on its business.

No lien or adjustment of such insurer's policies shall be made or imposed which has the effect of creating or making available for distribution to the shareholders of such insurer assets otherwise unavailable therefor.

(c) [*Regulating and adjusting rights of holders of policies of different classes, etc.*] Regulating and adjusting the respective rights of holders of policies of different classes to participate in the profits or savings which may be made by such insurer when mutualized.

(d) [*Regulating compensation of shareholders for interest other than goodwill.*] Regulating the manner in which and the time at which the shareholders of such insurer shall be compensated for their proprietary interest, then existing, in the assets of such insurer other than goodwill.

(e) [*Regulating compensation of shareholders for interest in goodwill.*] Regulating the manner in which the shareholders of such insurer shall be compensated for their proprietary interest in the goodwill, if then existing, of such insurer; provided, however, that no shareholder shall be compensated for his proprietary interest in such goodwill while any moratorium imposed under subdivision (a) of this section is in effect, nor while any lien imposed under subdivision (b) of this section exists, nor until all other indebtedness of such insurer existing at the time of mutualization has been fully paid and discharged or full provi-

sion made for its payment, nor otherwise than out of surplus earnings.

(f) [*Regulating other matters.*] Regulating such other matters as may, in the opinion of the commissioner, require regulation in the interest of expediency or otherwise.

§ 1048. SAME: APPLICATION FOR ORDER TO SUBMIT PLAN: ISSUANCE OF ORDER. Upon formulation of said mutualization plan the commissioner shall submit the same to said court with his application for an order of said court directing the commissioner to submit said mutualization plan to the persons named in subdivision (e) of section 1046, under such procedure as shall be set forth in the plan or prescribed by said court, for their approval or rejection, and the court shall issue such order.

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§ 1049. SAME: POLICYHOLDER ENTITLED TO ONE VOTE: WHEN PLAN DEEMED APPROVED OR REJECTED: CERTIFICATION OF REJECTION. Each policyholder of such insurer shall be entitled to one vote, regardless of the amount for which, or the number of policies under which, he is insured. Such mutualization plan shall be deemed approved by the said policyholders if a majority of the policyholders voting for and against it shall have approved it, and shall be deemed rejected if a majority of the policyholders voting for and against it shall have rejected it. In the event that said plan of mutualization is rejected by the policyholders of such insurer, the commissioner shall certify the fact of such rejection to said court, whereupon he may proceed further as hereinbefore provided in this article.

§ 1050. SAME: CERTIFICATION OF APPROVAL OF PLAN: ORDER DIRECTING GIVING NOTICE OF APPROVAL: PETITION BY SHAREHOLDER DISAPPROVING PLAN: PETITION FOR APPOINTMENT OF APPRAISERS. In the event that said plan of mutualization is approved by said policyholders, the commissioner shall certify to the said court the fact of such approval and the number of votes cast for and against such mutualization plan. Said court shall thereupon issue its order directing the commissioner to give notice, as provided in said mutual-

ization plan or as the court may otherwise prescribe, to the shareholders of such insurer of the approval of said mutualization plan by said policyholders. Said order shall direct the commissioner to transmit to each such shareholder by mail addressed to his address as it appears upon the records of such insurer, a true copy of said order and of said mutualization plan approved by said policyholders, and shall fix a time, not less than thirty nor more than sixty days from the date of such order, within which any such shareholder may file with said court a petition for the disapproval of said mutualization plan or for its modification in such manner, as shall be set forth in such petition, and within which any such shareholder and the commissioner may file with said court a petition for the appointment of one or more appraisers to appraise the value of the then outstanding shares of capital stock of such insurer.

§ 1051. SAME: NOTICE OF HEARINGS OF PETITIONS: PRECEDENCE OF PETITIONS: APPROVAL OR DISAPPROVAL OF PLAN: APPOINTMENT OF APPRAISERS: APPRAISEMENT. After the expiration of the time fixed in the order provided for in section 1050, and upon the filing of such petition, said court shall direct notice of a hearing of said petitions to be given to the commissioner and to such petitioners as are shareholders of such insurer. At such hearing, all petitions for the disapproval and all petitions for the modification of said mutualization plan shall be given precedence over all petitions for the appointment of one or more appraisers. Upon hearing of all such petitions for the disapproval and for the modification of said mutualization plan, said court shall either approve said mutualization plan or disapprove it or modify it in such manner and to such extent, not inconsistent with the provisions of this article, as to said court shall seem appropriate. In the event of the disapproval of said mutualization plan the court shall deny all petitions for the appointment of one or more appraisers. In the event of the approval or modification of said mutualization plan, the court shall, upon hearing of the petitions for the appointment of appraisers, appoint one or more appraisers, who shall appraise the then outstanding shares of the capital stock of such insurer, without regard to any apprecia-

tion or depreciation arising out of said mutualization plan as so approved or modified. Such appraisement shall fix the reasonable value of such shares of capital stock, including the goodwill, if any, of such insurer, and shall state the value, if any assigned to such goodwill; and if the appraisers shall have found that such insurer has no goodwill, such finding shall be stated. Such appraisement, when confirmed by said court, shall be final and conclusive.

§ 1052. SAME: COMPLETION OF MUTUALIZATION. Thereupon the commissioner shall:

(a) [*Payment to shareholders.*] Pay to each of such shareholders or his assignee or nominee, upon surrender of the shares held by such shareholder, the value of said shares so ascertained; subject, however, to the restrictions of subdivisions (d) and (e) of section 1047, and subject, also, to the terms and conditions of the mutualization plan as approved or modified.

(b) [*Appointment of directors.*] Appoint, with the approval of the court, the requisite number of directors in whom shall thereafter be vested the control and management of the assets and business of such insurer until their successors shall have been elected and qualified.

(c) [*Transference of property, etc., to proper officers.*] Transfer, upon the order of said court, to the appropriate officers appointed by such directors, the property, real and personal, and the books, records, accounts and papers of such insurer; provided, however, that the commissioner may retain, as a deposit, so much of such property as he deems necessary to defray additional costs and expenses incurred or to be incurred in connection with any proceeding under this article affecting such property or business.

§ 1053. SAME: CESSATION OF OFFICE BY DIRECTORS IN OFFICE: TERMINATION OF VOTING RIGHTS OF SHAREHOLDERS: STATUS OF MUTUALIZED INSURER: POWER TO ISSUE NONASSESSABLE POLICIES. Immediately upon the appointment of the directors as provided in subdivision (b) of section 1052, the directors theretofore holding office shall cease to hold office, and all rights of the shareholders of such insurer to vote at any

meeting of such insurer shall absolutely cease and such shareholders shall retain only such interest in such corporation or in the property or assets thereof as shall be provided in said mutualization plan, and such insurer shall thereupon be and become a mutual life insurer under such corporate name as may have been set forth in its charter, as amended, to be conducted not for profit, but solely for the mutual benefit, ratably, of all its policyholders, and shall, upon issuance to it by the commissioner of a certificate of authority, have power to issue nonassessable policies on a reserve basis subject to all provisions of law applicable to incorporated life insurers issuing non-assessable policies on a reserve basis, but shall be exempt from the provisions of Chapter 7, Part 2, Division 2 of this code.

§ 1054. SAME: EFFECT OF MUTUALIZATION UPON EXISTING SUITS, CONTRACTS AND RIGHTS: RIGHTS, POWERS AND DUTIES OF MUTUALIZED INSURER. Such insurer, after mutualization, shall be a continuation of the original insurer, and such mutualization shall not affect existing suits, rights or contracts except as provided in said mutualization plan as approved. Such insurer, after mutualization, shall exercise all the rights and powers and perform all the duties conferred or imposed by law upon insurers writing the classes of insurance written by it, and to protect rights and contracts existing prior to mutualization, subject to the effect of said mutualization plan.

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§1055. SAME: POWERS AND DUTIES OF COMMISSIONER AS TO MUTUALIZED INSURERS: ISSUANCE OF CERTIFICATE OF AUTHORITY. The commissioner shall exercise the powers and discharge the duties, concerning any insurer so mutualized, that are applicable to domestic insurers issuing policies of the same class. He shall issue a certificate of authority to transact the proper classes of insurance in this State to any insurer so mutualized which is solvent under Article 13, Chapter 1, Part 2, Division 1 of this code and which has fully complied with the laws of this State.

§ 1056. SAME: PAYMENT OF COSTS AND EXPENSES. All costs and expenses connected with proceedings for the mutual-

ization of such insurer shall be paid by the commissioner out of the funds of such insurer, whether or not mutualized, subject to the approval of said court.

2. Code of Civil Procedure of California

§ 1094.5. [*Inquiry into validity of administrative order or decision.*] (a) Where the writ is issued for the purpose of inquiring into the validity of any final administrative order or decision made as the result of a proceeding in which by law a hearing is required to be given, evidence is required to be taken and discretion in the determination of facts is vested in the inferior tribunal, corporation, board or officer, the case shall be heard by the court sitting without a jury. All or part of the record of the proceedings before the inferior tribunal, corporation, board or officer may be filed with the petition, may be filed with respondent's points and authorities or may be ordered to be filed by the court. If the expense of preparing all or any part of the record has been borne by the prevailing party, such expense shall be taxable as costs.

(b) The inquiry in such a case shall extend to the questions whether the respondent has proceeded without, or in excess of jurisdiction; whether there was a fair trial; and whether there was any prejudicial abuse of discretion. Abuse of discretion is established if the respondent has not proceeded in the manner required by law, the order or decision is not supported by the findings, or the findings are not supported by the evidence.

(c) Where it is claimed that the findings are not supported by the evidence, in cases in which the court is authorized by law to exercise its independent judgment on the evidence, abuse of discretion is established if the court determines that the findings are not supported by the weight of the evidence; and in all other cases abuse of discretion is established if the court determines that the findings are not supported by substantial evidence in the light of the whole record.

(d) Where the court finds that there is relevant evidence which, in the exercise of reasonable diligence, could not have been produced or which was improperly excluded

at the hearing before respondent, it may enter judgment as provided in subdivision (e) of this section remanding the case to be reconsidered in the light of such evidence; or, in cases in which the court is authorized by law to exercise its independent judgment on the evidence, the court may admit such evidence at the hearing on the writ without remanding the case.

(e) The court shall enter judgment either commanding respondent to set aside the order or decision, or denying the writ. Where the judgment commands that the order or decision be set aside, it may order the reconsideration of the case in the light of the court's opinion and judgment and may order respondent to take such further action as is specially enjoined upon it by law but the judgment shall not limit or control in any way the discretion legally vested in the respondent.

(f) The court in which proceedings under this section are instituted may stay the operation of the administrative order or decision pending the judgment of the court, (or until the filing of a notice of appeal from the judgment or until the expiration of the time for filing such notice whichever occurs first; provided that no such stay shall be imposed or continued if the court is satisfied that it is against the public interest.) If an appeal is taken from a denial of the writ, the order or decision of the agency shall not be stayed except upon the order of the court to which such appeal is taken; (provided that, in cases where a stay is in effect at the time of filing the notice of appeal, such stay shall be continued by operation of law for a period of twenty (20) days from the filing of such notice.) If an appeal is taken from the granting of the writ, the order or decision of the agency is stayed pending the determination of the appeal unless the court to which such appeal is taken shall otherwise order. Where any final administrative order or decision is the subject of proceedings under this section, if the petition shall have been filed while the penalty imposed is in full force and effect the determination shall not be considered to have become moot in cases where the penalty imposed by the administrative agency has been completed or complied with during the pendency of such proceedings.

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JAN 20 1956
CHARLES ELMORE CROPLEY, Clerk

IN THE

Supreme Court of the United States

OCTOBER TERM, 1955.

No. 584

FRANK GENTLES, *et al.*,

Appellants,

vs.

F. BRITTON McCONNELL, as Insurance Commissioner of the State of California, *et al.*,

Appellees.

No. 585

THE PACIFIC MUTUAL LIFE INSURANCE COMPANY OF CALIFORNIA, *et al.*,

Appellants,

vs.

F. BRITTON McCONNELL, as Insurance Commissioner of the State of California, *et al.*,

Appellees.

Appeal From the Supreme Court of the State of California.

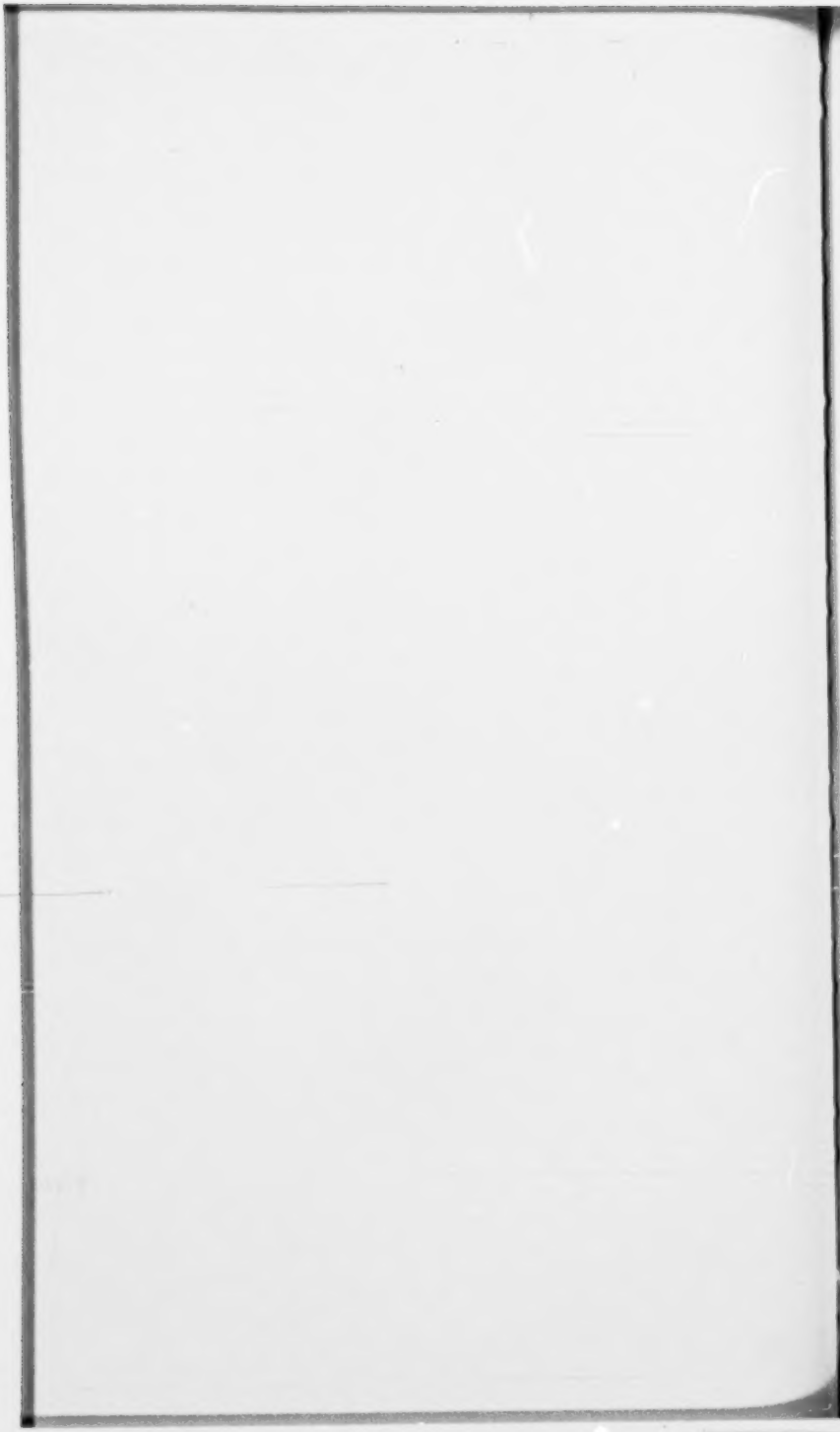
MOTION TO DISMISS.

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DARK PAGE BLEED THRU



SUBJECT INDEX

PAGE

Opinions below 2

Jurisdiction 2

Questions presented 3

Statement 3

Argument 11

I.

No state statute was challenged on federal grounds in the courts below, as required for jurisdiction under 28 U. S. C., Section 1257(2) 11

A. The validity of Sections 11525-11527 of the Insurance Code was not drawn in question in the court below..... 11

B. The Insurance Commissioner's action is not a "statute" within the meaning of Section 1257(2)..... 12

II.

There is no substantial federal question..... 15

A. The binding force of the Rehabilitation Agreement, including the stockholder's consent to the Plan of Mutualization, is res judicata in this court..... 15

B. The action of the Insurance Commissioner did not deprive appellants of property without due process of law 17

C. The proceedings below met every requirement of procedural due process..... 29

III.

There is no important or recurrent question of federal law involved 32

Conclusion 32

AGE BLEED THRU

TABLE OF AUTHORITIES CITED

Cases	PAGE
Alabama Public Service Commission v. Southern Ry. Co., 341 U. S. 341	30
American Trucking Assn. v. United States, 344 U. S. 298	30
Belden v. Union Central Life Ins. Co., 143 Ohio St. 329, 55 N. E. 2d 629	14
Brinkley v. Hassig, 83 F. 2d 351	31
Brock v. Superior Court, 109 Cal. App. 2d 594, 241 P. 2d 283	13
Carpenter v. Pacific Mutual Life Ins. Co., 10 Cal. 2d 307, 74 P. 2d 761	5
Carpenter v. Pacific Mutual Life Insurance Co., 13 Cal. 2d 306, 89 P. 2d 637	16
Case v. Los Angeles Lumber Products Co., 308 U. S. 106	16
Catholic Order of Foresters v. North Dakota, 301 U. S. 665	14
Champlin Refining Co. v. Ryan, 304 U. S. 549	14
Charleston Assn. v. Alderson, 324 U. S. 182	12
Chicago Life Ins. Co. v. Cherry, 244 U. S. 25	17
Chicot County District v. Baxter State Bank, 308 U. S. 371	17
Consolidated Rock Products Co. v. DuBois, 312 U. S. 510	20
Ecker v. Western Pacific R. Corp., 318 U. S. 448	30
Evans v. Gore, 253 U. S. 245	31
Federal Trade Commission v. Cement Institute, 333 U. S. 683	31
Grubb v. Public Utilities Commission, 281 U. S. 470	17
Hamilton v. Liverpool etc. Ins. Co., 136 U. S. 242	18
Hamilton v. Regents of the University of California, 293 U. S. 245	12
King Mfg. Co. v. Augusta, 277 U. S. 100	12, 13
Latshaw v. Missouri ex rel. Kansas City Public Service Co., 282 U. S. 806	14
Memphis Natural Gas Co. v. Beeler, 315 U. S. 649	12, 17

PAGE

Neblett v. Carpenter, 305 U. S. 297 ..... 3, 4, 5, 15, 29
New York Title Mortgage Co., Matter of, 171 Misc. 489, 13 N. Y. S. 2d 214 22
Ohio v. Baxter, 332 U. S. 827 14
Ohio Valley Co. v. Ben Avon Burrough, 253 U. S. 287 30
Omaha v. Omaha Water Co., 218 U. S. 180 18
Railroad Commission of Texas v. Rowan & Nichols Oil Co., 311 U. S. 570 30
Rice v. Sioux City Memorial Park Cemetery, Inc., 349 U. S. 70 32
St. Joseph Stockyards Co. v. United States, 298 U. S. 38 30
Schmidt v. Minnesota State Board, 311 U. S. 617 14
Securities and Exchange Commission v. Central Illinois Securities Corp., 338 U. S. 96 30
Securities and Exchange Commission v. Chenery Corp., 332 U. S. 194 29
Standard Scale Co. v. Farrell, 249 U. S. 571 ..... 14, 19
Stoll v. Gottlieb, 305 U. S. 165 17
United States v. Moorman, 338 U. S. 457 18
Wilson v. Cook, 327 U. S. 474 12

RULES

Revised Rules of the United States Supreme Court, Rule 16(1) 1

STATUTES

California Code of Civil Procedure, Sec. 1094.5 ..... 9, 13, 31
California Insurance Code, Sec. 1011 4
California Insurance Code, Sec. 1013 4
California Insurance Code, Sec. 1043 4
California Insurance Code, Sec. 11525 ..... 11, 13
California Insurance Code, Sec. 11526 ..... 8, 11
California Insurance Code, Sec. 11527 ..... 8, 11, 28, 31

RK PAGE BLEED THRU

PAGE

United States Code, Title 28, Sec. 1257(2).....2, 3, 11, 12, 14, 19
United States Code, Title 28, Sec. 2103..... 32
United States Constitution, Fourteenth Amendment.....17, 29, 31

TEXTBOOKS

Badger, Valuation of Industrial Securities..... 23
Bonbright, Valuation of Property, p. 239.....23, 26
Dewing, The Financial Policy of Corporation..... 23
Finletter, Principles of Corporate Reorganization, p. 498..... 26

IN THE

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THE PACIFIC MUTUAL LIFE INSURANCE COMPANY OF CALIFORNIA, *et al.*,

Appellants,

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F. BRITTON McCONNELL, as Insurance Commissioner of the State of California, *et al.*,

Appellees.

Appeal From the Supreme Court of the State of California.

MOTION TO DISMISS.

Appellee Pacific Mutual Life Insurance Company moves pursuant to Rule 16(1) of the Revised Rules of the Supreme Court that the appeal from the final judgment of the Supreme Court of California be dismissed for want of jurisdiction on the following grounds: (1) That the appeal was not taken in conformity to statute in that there was not drawn into question in the courts below the validity of any state statute on the ground of its being repug-

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nant to the Constitution, treaties, or laws of the United States, as required by 28 U. S. C., Section 1257(2); (2) That the federal questions sought to be reviewed were not timely or properly raised or expressly passed upon; (3) That the appeal does not present any substantial federal question; and (4) That the judgment rests on an adequate non-federal basis.

Opinions Below.

The opinions in the Supreme Court of California (App. pp. A1-A69)* are reported in 44 Cal. 2d 715, 285 P. 2d 636. The opinion of the District Court of Appeal of California, First Appellate District (App. pp. B1-B36) is reported at 270 P. 2d 584. The opinion of the Superior Court for Los Angeles County (App. pp. C1-C34), and the opinion and decision of the California Insurance Commissioner (App. pp. D1-D22) are not reported.

Jurisdiction.

The judgment of the Supreme Court of California (App. pp. H1-H2) was filed on June 27, 1955, and the petition for rehearing was denied without opinion on July 27, 1955. Notice of appeal was filed on October 24, 1955. The jurisdiction of this Court is sought to be invoked under Section 1257(2) of the Judicial Code (U. S. C., Title 28, Sec. 1257(2)).

Jurisdiction is challenged by this Motion.

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*References to the Appendix throughout this Motion are to the volume filed by appellants in No. 584. References to the record lodged with the Clerk will follow the pattern stated in the Jurisdictional Statement of appellants in No. 584 at page 5n.

Questions Presented.

In *Neblett v. Carpenter,* 305 U. S. 297, this court reviewed and sustained a Rehabilitation Agreement which obligated the sole stockholder of a California insurance company to dispose of his stock in accordance with a Plan of Mutualization thereafter to be formulated by a committee of insurance experts. Such a Plan was formulated and, after full hearing, approved by the State Insurance Commissioner, thus permitting but not requiring the Plan to become effective. Appellants, claiming through the sole stockholder, brought mandamus to review the Commissioner's action. The questions presented are:

1. Was there drawn in question in the courts below the validity of any state statute on the ground of its repugnance to the Constitution, treaties or laws of the United States as required for jurisdiction on appeal in this Court under 28 U. S. C., Sec. 1257(2)?

2. Did the action of the Insurance Commissioner in approving the Plan of Mutualization or the judicial review thereof in the California courts deprive Appellants of property without due process of law?

Statement.

We believe a statement of the case is warranted because the Jurisdictional Statements filed by Appellants do not present the case accurately or completely, from either a factual or legal standpoint. They state the case as though Appellants' rights as stockholders were before the courts for the first time in the present litigation. Quite the contrary is true. The facts as found by the Insurance Commissioner and as accepted by the courts below may be summarized as follows:

GE BLEED THRU

For many years before 1936 Appellant The Pacific Mutual Life Insurance Company of California ("Old Company") was a stock company engaged in writing life, accident and health insurance (App. p. D1). In 1936 an insurance commissioners' audit found Old Company to be in a hazardous and insolvent condition within the meaning of the Insurance Code of California (App. p. B6). The insolvency arose out of the fact that many non-cancellable accident and health policies ("non-can policies") had been issued with inadequate premium rates, and when reserves on the non-can business were required to be set up on a realistic basis, the capital and surplus of the Company were entirely wiped out and there was a deficit of at least $17,000,000 (App. p. D1). Acting pursuant to Sections 1011 and 1013 of the California Insurance Code, the Insurance Commissioner seized Old Company and was appointed Conservator on July 22, 1936 (App. p. A2).*

To preserve the outstanding insurance business, the agency organization and the good will of Old Company, the Commissioner as Conservator organized, with court approval, Appellee Pacific Mutual Life Insurance Company ("New Company") (App. p. D2). Pursuant to Section 1043 of the Insurance Code, the Commissioner as Conservator thereupon submitted to the Superior Court for approval a Rehabilitation and Reinsurance Agreement ("Rehabilitation Agreement") with New Company.

In December, 1936, after a full hearing at which all parties were represented, including Old Company and its

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*The judge who entered the original order overlooked the fact that he owned a policy issued by the Company and that he was therefore disqualified. On August 11, 1936, another judge entered an order which ratified, approved and confirmed the Commissioner's seizure of Old Company and the appointment of the Commissioner as Conservator. See *Neblett v. Carpenter*, 305 U. S. 297, 300.

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stockholders, the Superior Court entered an order "approving the Commissioner's plan and agreement, ratifying the action he had taken, and authorizing him as conservator, and as liquidator, if he should be appointed as such, to carry out the rehabilitation agreement". *Neblett v. Carpenter,* 305 U. S. 297, 301. "The order of the Superior Court recites that the plan [the Rehabilitation Agreement] makes adequate provision for each class of policy holders, for the creditors, and for the stockholders; that the plan is fair and equitable; . . . and that if the old company were dissolved and its assets sold their value would be substantially less than the amount which will be realized from them under the plan." 305 U. S. at 304. The Rehabilitation agreement was executed by the parties as of December 4, 1936. The order of the Superior Court was affirmed on appeal by the Supreme Court of California (*Carpenter v. Pacific Mutual Life Ins. Co.,* 10 Cal. 2d 307, 74 P. 2d 761), and on certiorari by this Court. *Neblett v. Carpenter,* 305 U. S. 297. The binding force of the Rehabilitation Agreement and all of its provisions was finally adjudicated in that proceeding.

Pursuant to the Rehabilitation Agreement the Conservator transferred substantially all of the assets of Old Company to New Company. The capital stock of New Company was held by him for the benefit of the creditors, policyholders and stockholders of Old Company. New Company on its part reinsured Old Company's non-can policies on a reduced schedule of benefits and all of Old Company's other policies without reduction of benefits. The Rehabilitation Agreement also provided for the ultimate restoration of full non-can benefits from future earnings of New Company not reasonably required for the operation of New Company as a going concern. The

GE BLEED THRU

participating life policyholders of Old Company contributed $3,000,000 for the capital and surplus of New Company and in addition $1,792,118.97 to strengthen non-can reserves (App. p. B7).* The stockholders of Old Company contributed no new money or other new assets to New Company.

The Rehabilitation Agreement also contained detailed provisions for an option to mutualize New Company at the instance of its participating life policyholders.** It provided (App. pp. F24, *et seq.*) that after July 1, 1946, ten per cent of the holders of participating policies of life insurance in New Company could request the creation of an Appointing Committee consisting of the President of the Life Insurance Association of America, the President of Stanford University, and the Provost of the University of California at Los Angeles. That Committee in turn was directed to appoint a Price Determination Committee of from three to five persons "skilled in matters of insurance company valuation" (App. p. F25). The Price Determination Committee was to determine whether mutualization "can then be practicably accomplished," and if so, it was then to "determine the proper price to be paid upon such mutualization and appropriate terms of payments thereof" (App. pp. F25-F26). The Insurance Commissioner, as sole stockholder of New Company, by the terms of the Rehabilitation Agreement, "agrees to

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*As of December 31, 1948, the participating life policyholders had supplied an additional $2,005,640 to the funds of New Company for its general corporate purposes, pursuant to the provisions of the Rehabilitation Agreement (Ex. 28, p. 13a; see App. p. F8).

**Participating life policyholders have by far the largest stake in New Company. Of the Company's $361,509,000 liabilities, as of the end of 1949, $224,336,000 were liabilities to participating life policyholders (Ex. 40).

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consent and hereby consents as the holder and owner of the stock of New Company to such plan of mutualization" and to "dispose of such stock in accordance with such Plan" in the event it is adopted (App. p. F27).

In 1946 the participating life policyholders, in accordance with the provisions of the Rehabilitation Agreement, initiated steps to exercise their option to mutualize the Company. The Appointing Committee designated a Price Determination Committee made up as follows: Alva J. McAndless, President of Lincoln National Life Insurance Co., Ray D. Murphy, Vice President and Chief Actuary of The Equitable Life Insurance Society of the United States, Horace R. Bassford, Vice President and Chief Actuary of the Metropolitan Life Insurance Company, and Albert J. Hettinger, an investment banker who was formerly professor of business economics at the Harvard School of Business Administration and had specialized in the valuation of insurance company stocks. The Committee employed as its Chief Actuary Joseph J. Christman, Associate Actuary of the Metropolitan Life Insurance Company. The background and experience of the Committee is set forth in detail in the opinion of the District Court of Appeal (App. pp. B16-B18).

After a study lasting over three years, the Price Determination Committee determined that mutualization could be practicably accomplished and prepared a detailed plan of mutualization (App. pp. G1-G30). That Plan fixed the price for the stock to be made up of three elements: $3,000,000 plus interest from December 31, 1948, plus augmentation of $250,000 per year for each year by which restoration of non-can benefits should be accomplished before December 31, 1973. (App. pp. G5-G6.)

PAGE BLEED THRU

The Company was obligated to pay this price when full restoration of the non-can benefits was completed and certain specified financial requirements of New Company were attained (App. pp. G6-G9).

Each step of the statutory procedure for voluntary mutualization (Secs. 11526-7 of the California Insurance Code, App. pp. E10-E12) was followed. The proposed Plan of Mutualization was submitted to and adopted by the Board of Directors of New Company (App. p. A3). Stockholder approval had been given by the Rehabilitation Agreement (*ibid.*). Since the Rehabilitation Agreement provided (App. p. F24) that the mutualization should be in accordance with the laws of California in effect at the time of the request for the creation of the Appointing Committee, the Plan was presented to the Insurance Commissioner. Section 11527 provides:

> "The Commissioner shall examine the plan submitted to him under the provisions of subdivision (c) of section 11526. He shall not approve such plan unless in his opinion the rights and interests of the insurer, its policyholders and shareholders are protected nor unless he is satisfied that the plan will be fair and equitable in its operation."

The Insurance Commissioner held a hearing upon notice to all interested parties and all persons desiring to be heard were heard (App. pp. B20-B21). By testimony and comprehensive exhibits, two members of the Price Determination Committee and its Chief Actuary explained in detail the bases upon which the Plan, including the

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price and terms of payment, had been formulated (App. pp. C11-C13). Thereafter the Commissioner approved the Plan, finding that the rights and interests of New Company, its policyholders and the holder of its shares were protected and that the Plan would be fair and equitable in its operation (App. pp. D1-D22). Following his approval, the Plan was submitted to and approved by the New Company life policyholders (App. p. A4).

Appellants, Old Company and its stockholders, petitioned the Superior Court for a writ of mandamus to review the Insurance Commissioner's decision, as provided in Section 1094.5 of the California Code of Civil Procedure (App. pp. E12-E14). That court, upon all of the records of the proceedings before the Insurance Commissioner, concluded that the Commissioner had not exceeded his jurisdiction, that he had accorded a fair hearing to all parties, and that his approval of the Plan was supported by substantial evidence. Judgment was entered denying the petition for mandamus (App. pp. C1-C34). The District Court of Appeal unanimously affirmed the judgment (App. pp. B1-B36). The Supreme Court of California, by a majority vote, did likewise (App. pp. A1-A69).

The majority opinion in the court below (Gibson, C. J.) (App. pp A1-A16) held, first, that the proper section of the Insurance Code of California had been followed in the formulation and approval of the mutualization plan, basing its decision both on an analysis of the statutes themselves, and on the ground that the issue was *res*

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judicata because the mutualization procedure had been specified in the Rehabilitation Agreement which had been adjudicated valid in the earlier litigation. Second, the court held that the appropriate sections of the Insurance Code had been fully complied with. Specifically, it concluded that the stockholders had properly consented by virtue of the advance consent of the Commissioner as Liquidator given by the Rehabilitation Agreement, basing its conclusion again both on the law of California and on the fact that the validity of that consent embodied in the Rehabilitation Agreement was *res judicata*. Third, the court held that the action of the Commissioner in approving the Plan was based on substantial evidence and was proper and valid. Finally, the court held that in view of the nature of the action of the Commissioner, the law of California did not require a trial *de novo* before the Superior Court, and was properly limited to a determination whether the action taken by the Commissioner was arbitrary or constituted an abuse of discretion.

Justice Traynor dissented (App. pp. A16-A21) on the ground that California statutes required court approval of the Plan of Mutualization, and that the order authorizing the Rehabilitation Agreement, as he construed it, did not eliminate the necessity for such approval. Justice Carter dissented (App. pp. A21-A69) on the ground that the action was taken under the wrong statutes and was therefore void, that *res judicata* consequently had no application, and that the Plan of Mutualization was unfair and should be disapproved. Justice Schauer concurred in the opinion of Justice Traynor, and concurred generally in the opinion of Justice Carter.

A petition for rehearing, filed on June 17, 1955, was denied without opinion on July 17, 1955.

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ARGUMENT.

I.

No State Statute Was Challenged on Federal Grounds in the Courts Below, as Required for Jurisdiction Under 28 U. S. C., Section 1257(2).

Both Jurisdictional Statements assert two separate bases of jurisdiction for this appeal under Section 1257(2): first, that the validity of the mutualization provisions of the California statutes (Secs. 11525-11527 of the Insurance Code), as construed and applied, is involved; and second, that the action of the Insurance Commissioner is a "statute" within the meaning of Section 1257(2). Neither basis can be sustained.

A. The Validity of Sections 11525-11527 of the Insurance Code Was Not Drawn in Question in the Court Below.

The short answer to the first alleged basis for jurisdiction is simply that the validity of Sections 11525-11527 of the Insurance Code of California was not "drawn in question" on federal grounds in the California courts. The Petition for Mandate by which these proceedings were begun in the California Superior Court contains only one reference to the Fourteenth Amendment:

> "Said Findings and order of said Commissioner deprive petitioners, and each of them, of property without due process of law, contrary to the provisions of the Constitution of the State of California and the Fourteenth Amendment to the Constitution of the United States" (Par. XXII, Clk. Tr. 22).

The briefs filed below which have been lodged with the Clerk show Appellants made no challenge to the constitutional validity of the Insurance Code in the California

GE BLEED THRU

courts. The opinions in the courts below do not pass on any such issue.

It is too late for Appellants to challenge the validity of the California Insurance Code for the first time in this Court. It is essential to this Court's jurisdiction on appeal under Section 1257(2), that "there be an explicit and timely insistence in the state courts that a state statute, as applied, is repugnant to the federal Constitution, Treaties or laws". *Charleston Assn. v. Alderson,* 324 U. S. 182, 185; see *Memphis Natural Gas Co. v. Beeler,* 315 U. S. 649, 650-651. Appellants' failure to challenge on federal grounds the sections of the Insurance Code is not cured by objection to the action of the Insurance Commissioner under the statute; "the mere objection to an exercise of authority under a statute, whose validity is not attacked, cannot be made the basis" of an appeal. *Wilson v. Cook,* 327 U. S. 474, 482.

B. The Insurance Commissioner's Action Is Not a "Statute" Within the Meaning of Section 1257(2).

The action of the Insurance Commissioner, the validity of which was drawn in question on federal grounds below, does not constitute a "statute of any state" within the meaning of 28 U. S. C., Section 1257(2). While the term "statute" has been interpreted over the dissents of Justices Holmes and Brandeis to apply to city ordinances and certain administrative orders, state action must nevertheless, as the Supreme Court said, be "legislative in character" to fall within Section 1257(2). *King Mfg. Co. v. Augusta,* 277 U. S. 100, 104-105; *Hamilton v. Regents of the University of California,* 293 U. S. 245, 258. In the *King* case, the court emphasized that "unlike other state action, legislation consists of rules having continu-

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ing force and intended to be observed and applied in the future . . ." *King Mfg. Co. v. Augusta,* 277 U. S. at 104.

In no sense whatever is the Insurance Commissioner's action in approving the Plan of Mutualization "legislative in character." The courts below did not so regard it (App. pp. A14, B34).* The Commissioner's action compelled nothing (App. p. D22). It did not "order"** anyone to do anything. It was but a step (and not even the final one, since the Plan had thereafter to be approved by the policyholders) in a series of approvals which allows the company to purchase its own stock.*** Moreover, his action had no general or continuing force, it was not intended to be applied in the future, and even for the one transaction with which it was con-

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*Indeed, Section 1094.5 of the California Code of Civil Procedure, under which the Commissioner's action was reviewed below, is not available to review legislative or quasi-legislative action. *Brock v. Superior Court,* 109 Cal. App. 2d 594, 598, 241 P. 2d 283, 286-287 (1952).

**Appellants persistently mislabel the Commissioner's action in approving the Plan as an "order." The Commissioner's action contains no ordering provision and the California Supreme Court never referred to it as an order but on the contrary uniformly and meticulously referred to it as the "action" of the Commissioner. Moreover, the District Court of Appeal emphasized that "Even after the Commissioner's approval the life policyholders could have rejected the plan, had they so desired. The stockholder could have rejected the plan but for the Rehabilitation and Reinsurance Agreement, which obligated the stockholder to dispose of the stock at the price and upon the terms fixed by the Price Determination Committee. The compulsion upon the stockholder flows from the obligations of the Rehabilitation and Reinsurance Agreement and not from the Commissioner's approval of the plan" (App. pp. B34-B35).

***The Statement as to Jurisdiction in No. 585 itself points out, page 9, "A plan of voluntary mutualization adopted in accordance with Secs. 11525, *et seq.* is not binding on either the Company or the stockholders. The Company may refuse to buy or the stockholders may refuse to sell."

E BLEED THRU

cerned, it did not determine any policy or fix any legal principles. It says in effect: "I find nothing wrong with the plan from any official standpoint; the Company may, therefore, proceed with the remaining steps to voluntary mutualization."

In view of the nature of the Commissioner's action, it falls outside of this Court's jurisdiction on appeal within the rule of such cases as *Ohio v. Baxter,* 332 U. S. 827 (Planning Commission's denial of zoning permit not a "statute"); *Schmidt v. Minnesota State Board,* 311 U. S. 617 (appeal dismissed from order of State Board suspending license to practice medicine for five years); *Champlin Refining Co. v. Ryan,* 304 U. S. 549 (order of state Secretary of State fixing annual franchise tax in accordance with statutory formula not a "statute"); *Catholic Order of Foresters v. North Dakota,* 301 U. S. 665 (appeal dismissed from order of state commission calling in bonds before redemption date); *Latshaw v. Missouri ex rel. Kansas City Public Service Co.,* 282 U. S. 806 (order of rate making body directing appraisal and audit preliminary to rate hearing not a "statute"); see *Standard Scale Co. v. Farrell,* 249 U. S. 571, 577 (specification of State Superintendent of Weights and Measures not a "regulation purporting to prescribe a course of action to be enforced by the power of the state").*

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*Whether the California Commissioner's action is a "statute" under Sec. 1257(2) is not controlled by decisions from other states involving proceedings for mutualization under other statutes, as Appellants contend (No. 584, p. 22n; No. 585, p. 42). Moreover, the decisions cited by Appellants do not support their text. In the only case remotely similar to the present one—*Belden v. Union Central Life Ins. Co.,* 143 Ohio St. 329, 56 N. E. 2d 629 (1944)—the court held that a statute authorizing a superintendent of insurance to approve or disapprove a mutualization plan "does not delegate legislative power." 56 N. E. 2d at p. 638.

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II.

There Is No Substantial Federal Question.

A. The Binding Force of the Rehabilitation Agreement, Including the Stockholder's Consent to the Plan of Mutualization, Is Res Judicata in This Court.

The rehabilitation of the business of the Pacific Mutual Life Insurance Company was before this Court in *Neblett v. Carpenter,* 305 U. S. 297. In that case, this Court upheld the 1936 order of the California Supreme Court approving the seizure of the assets of Old Company and adjudicating valid and directing performance of the Rehibilitation Agreement. The entire modification of Appellants' property rights took place at that time through the Rehabilitation Agreement. The California Supreme Court has held that the validity of the entire Rehabilitation Agreement is *res judicata* as to all parties, including the stockholders of Old Company (App. pp. A8-A12). The Insurance Commissioner's action merely allows the carrying out of that Agreement. There is no substantial federal question presented for adjudication.

As a result of the prior litigation adjudicating valid the Rehabilitation Agreement, the following matters are *res judicata* under the decision of the court below:

(a) The Insurance Commissioner was authorized in 1936 to organize New Company, to become its sole stockholder, and to transfer the assets of Old Company to New Company;

GE BLEED THRU

(b) The stock of New Company is held by the Liquidator* subject to an option under which a Price Determination Committee shall determine whether mutualization is practicable and, if so, shall formulate a Plan of Mutualization and shall determine the price to be paid for the stock of New Company and the terms of payment;

(c) The Liquidator as sole stockholder of New Company is obligated to dispose of his stock in accordance with the Plan; and

(d) The stockholders of Old Company, Appellants here, have an equitable right to receive from the Liquidator so much of the proceeds of the sale of New Company's stock as is left after the payment of creditors.**

This application of *res judicata* raises no substantial federal question. Even an erroneous decision on *res judicata* is not a violation of due process, for, as Justice Holmes said, "if a mistake [in the application of *res judicata*] is not so gross as to be impossible in a rational administration of justice, it is no more than the imperfection of men, not a denial of constitutional rights". *Chi-*

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*On February 2, 1937, the court, in the conservatorship proceedings, ordered the liquidation of Old Company and appointed the Insurance Commissioner as Liquidator. The validity of the order was upheld on appeal (*Carpenter v. Pacific Mutual Life Insurance Co.*, 13 Cal. 2d 306, 89 P. 2d 637 (1939)). Thus the Liquidator succeeded the conservator as the sole stockholder of New Company. Said stockholder will hereinafter be referred to as the Liquidator.

**The equitable rights of Appellants as stockholders of Old Company arise solely from the Rehabilitation Agreement. Since they contributed no new money or new assets to New Company (see *supra*, pp. 5-6), and since Old Company was insolvent, they would have been eliminated entirely but for the Agreement if the rule of absolute priority of *Case v. Los Angeles Lumber Products Co.*, 308 U. S. 106, had been applied.

DARK PA

cago Life Ins. Co. v. Cherry, 244 U. S. 25; see also, *Angel v. Bullington,* 330 U. S. 183; *Stoll v. Gottlieb,* 305 U. S. 165, 172. No argument is necessary to demonstrate that the decision below on *res judicata* does not pass Justice Holmes' line; indeed, it is manifestly correct. Moreover, despite Appellants' suggestion to the contrary (No. 585, pp. 21-22), it is well settled that constitutional issues, equally with other issues, can be foreclosed by *res judicata. Chicot County District v. Baxter State Bank,* 308 U. S. 371; *Angel v. Bullington,* 330 U. S. 183; *Grubb v. Public Utilities Commission,* 281 U. S. 470.

Thus, the basic questions sought to be raised in the Jurisdictional Statements are not open here because they have been decided on an adequate non-federal ground—*res adjudicata.* Moreover, the holding below that the Plan of Mutualization, and the Commissioner's approval thereof, are in accordance with the Rehabilitation Agreement is a matter of state law and raises no question here. *Memphis Gas Co. v. Beeler,* 315 U. S. 649, 654. Despite all this, in an attempt to salvage something, Appellants seek to create a constitutional issue by charging that the action of the Commissioner in giving his approval to the Plan of Mutualization violates the Fourteenth Amendment. Appellants' efforts are wholly unsuccessful.

B. The Action of the Insurance Commissioner Did Not Deprive Appellants of Property Without Due Process of Law.

The lack of substance in the claim that the action of the Insurance Commissioner deprived Appellants of their property without due process of law may be demonstrated in several ways.

First, the action of the Insurance Commissioner did not deprive Appellants of "the ordinary right of a prop-

E BLEED THRU

erty owner to determine when he will sell and for how much" (No. 584, p. 26) or any other right. Appellants are stockholders of Old Company, and they have the right to sell that stock at any time they see fit. They do not own the New Company stock. The stock of New Company is owned by the Liquidator and Appellants' equitable rights in that stock have been defined by and are subject to the obligations of the Rehabilitation Agreement. Appellants' right under that Agreement is to receive the proceeds (after payment of creditors) from the sale of the stock of New Company at the price and upon the terms of payment determined by the Price Determination Committee. The Plan of Mutualization approved by the Commissioner preserves this property right intact.* In the litigation nearly twenty years ago when the Rehabilitation Agreement itself was before the courts, Appellants had their opportunity to challenge the validity and propriety of the provisions of that Agreement which bound them to accept the value placed on the stock by a Price Determination Committee. There is no constitutional issue created when parties bind themselves to accept a price or valuation to be determined by appraisers appointed in accordance with a contract. *Hamilton v. Liverpool etc. Ins. Co.,* 136 U. S. 242, 255; *Omaha v. Omaha Water Co.,* 218 U. S. 180, 193-198; see *United States v. Moorman,* 338 U. S. 457, 460-462.

Second, since the Commissioner's action is "not in the nature of a law or regulation, the prohibitions of the

*The District Court of Appeal emphasized that "The basic problem for the Commissioner to determine was whether or not the price and terms of payment for the New Company stock were fixed in accordance with the Rehabilitation Agreement, for if they were, the Plan of Mutualization is fair and equitable because it gives the stockholder the price and terms he agreed to take." (App. pp. B33-B34).

DARK P

Federal Constitution cannot apply." *Standard Scale Co. v. Farrell,* 249 U. S. 571, 577. The action of the Commissioner was not in any sense an order or command which could or did deprive Appellants of any property whatever. The action he took was to approve what the parties had agreed to. We urge above (*supra,* pp. 12-14), that such an action cannot possibly be classed as a "statute" within the meaning of 28 U. S. C. Section 1257(2). We say here that neither can it possibly create a substantial claim of taking of property without due process of law. As the District Court of Appeal correctly stated,

> "On this question of due process we should never lose sight of the fact that the commissioner's approval of the Plan of Mutualization did not have the effect of taking appellants' property, since it was nothing more or less than a permit and did not compel the life policyholders to approve the plan, nor the stockholder to dispose of the stock as therein provided, or the New Company to adopt the plan." (App. p. B34.)

The California Supreme Court reached the same conclusion. (App. p. A14.)

Third, and in any event, there is no basis whatever for the claim that the Commissioner's action was arbitrary and capricious or that it was not supported by substantial evidence. Three California courts have extensively reviewed and approved the action of the Commissioner, which should make it unnecessary for this Court to examine this lengthy record. Moreover, the charge that the Commissioner's action lacks "substantial evidence" verges on the fantastic in view of the fact that it is supported by the detailed and uncontradicted testimony of

GE BLEED THRU

two members of the Price Determination Committee and its Chief Actuary, and by comprehensive exhibits showing the basis of and the reasons for the conclusions of the Committee. However, in view of the charges made in the Jurisdictional Statement, it may be appropriate to review briefly the substantial evidence before the Commissioner which fully justified his conclusions.

Capitalization of Earnings. The uncontradicted evidence before the Commissioner showed that the Price Determination Committee valued the stock by determining its commercial or investment value.* The Committee made what Chairman McAndless testified was "one of the most complete investigations of earning power that has ever been made for any life insurance company", devoting to it approximately three years of time and 10,000 man-hours of work (Tr. pp. 134-135). Taking into account the Company's estimated future growth and other relevant factors, it projected earnings of the Company into the future (Tr. pp. 147-149).** Since under the Rehabilitation Agreement the stockholders had no claim to the earnings of the Company until after non-can benefits had been restored, "the key to determining the value of the stock was the determination of how many years' earnings would be required to restore non-can benefits (Tr. pp. 138-

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*The method used by the Committee was that advocated by Professor J. L. Bonbright in his authoritative treatise "Valuation of Property," cited with approval in *Consolidated Rock Products Co. v. DuBois*, 312 U. S. 510, 526. The Committee tested other possible methods of valuation and found that none would produce any value whatever for stock of New Company [Tr. pp. 141-147, 382-383, 385; Ex. 28, p. 24].

**In determining future earnings as a basis for commercial or investment value, "an estimate, as distinguished from mathematical certitude, is all that can be made." *Consolidated Rock Products Co. v. DuBois*, 312 U. S. 510, 526.

DARK P

139). Accordingly, the Committee determined the amounts which would be necessary to restore non-can benefits and the number of years' earnings which would be required to accomplish that restoration.* They concluded that it would consume all of the Company's earnings not required for its profitable operation until the middle of 1974 (Ex. 28, pp. 3-7; Tr. pp. 149, 152).** Consequently, the Committee then considered that earnings subsequent to 1974 should be capitalized in determining the value of the stock. Applying an appropriate rate of capitalization (*infra,* p. 23), the Committee concluded that the value of the stock as of December 31, 1948, was $3,000,000 (Tr. pp. 149-150).*** The procedure thus adopted, described in detail in Exhibit 28, was anything but "speculation and guesswork" (No. 584, pp. 4, 33; No. 585, pp. 14, 19), and the Insurance Commissioner was fully justified in accepting this uncontradicted evidence of value.

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*Appellants go outside the record to attack the Committee's estimate of the period of time necessary for non-can restoration (No. 584, p. 34). Even if Appellants' figures for 1950, 1951, and 1952 were correct (and they are grossly erroneous), the argument based on such figures is an application of hindsight and cannot serve to impugn the validity of the Commissioner's determination on the basis of the record before him.

**The Committee determined that an additional reserve of $22,000,000 as of December 31, 1948, invested at 3% compound interest, would permit the gradual complete restoration of non-can benefits. To equate future earnings to the $22,000,000 figure and thus enable the Committee to determine how many years' earnings would be required, it was necessary to discount those earnings at the same 3% rate. The Committee applied no discount for the risk that these earnings might not emerge, as would have been required to capitalize these earnings (Ex. 28, pp. 6-7; Tr. p. 149). These facts make it clear that Appellants err in treating the $22,000,000 as the "value of the stream of earnings" from 1949 to 1974. (No. 584, p. 14.)

***This value takes into account certain earnings from participating insurance, as required by the Rehabilitation Agreement (App. p. F26).

GE BLEED THRU

Valuation as of 1948. Appellants contend that the Committee should have determined the value of the stock as of 1974 (No. 584, pp. 4, 24-25; No. 585, pp. 22-23, 25-26, 48). However, the Committee determined the value as of December 31, 1948. The decisions of the California courts holding that the Committee proceeded in accordance with the Rehabilitation Agreement have necessarily construed the Agreement as authorizing the Committee to make the valuation as of 1948.

Moreover, the stock was properly valued as of 1948, because under the Plan the Company as of that date has an obligation to pay for the stock at the time and upon the conditions stated in the Plan.* When the Plan becomes effective the Liquidator will dispose of his stock by transferring it to new voting trustees, and thereupon New Company will be obligated to pay the purchase price including interest from December 31, 1948, at the time and upon the conditions specified in the Plan. Having disposed of the stock, the Liquidator and those claiming under him will have no further right to the subsequent earnings of New Company; the voting trustees will hold the stock as security for the payment of the purchase price, and beneficial interest in the stock will be in the life policyholders of New Company. The Liquidator's right will be analogous to that of a seller who has taken a purchase money trust deed to secure payment of the purchase price.

To estimate earnings from 1974 on and then to attempt to determine their value in 1974 by discounting them to that date, as advocated by Appellants, means that the

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*The Plan did not provide for an option as was the case in *Matter of New York Title Mortgage Co.*, 171 Misc. 489, 13 N.Y.S. 2d 214, cited by Appellants (No. 584, p. 25).

risk between 1948 and 1974 that distant earnings will not emerge as predicted would be thrust upon the life policyholders instead of being borne by Appellants who improvidently caused the non-can deficit which prevents earlier payment.

Capitalization Rate. The Committee determined upon a 10 per cent capitalization rate after taking into consideration the rate at which the market capitalizes the earnings of other life insurance corporations and after a study of authoritative texts such as Bonbright: "The Valuation of Property," Dewing: "The Financial Policy of Corporation," and Badger: "Valuation of Industrial Securities" (Ex. 28, p. 12; Tr. pp. 507, 382-389). This 10 per cent rate for valuing estimated earnings to emerge many years in the future is very favorable to Appellants, since the evidence showed that in valuing the stock of the leading life insurance companies the market was discounting their *current* earnings at rates of from 12.8 per cent to 23 per cent. As Mr. Hettinger testified:

> "I know of no market that I believe would apply as low rates of discount to future earnings as those we have employed." (Tr. p. 397.)

The proper rate of discount to be applied in valuing future earnings is an appropriate subject for expert testimony, and the Commissioner was not arbitrary, as Appellants suggest (No. 585, pp. 21-22), in accepting the uncontradicted testimony of the qualified experts who appeared before him.

Augmentations. The Plan provides that if complete restoration of non-can benefits precedes 1973, the price to be paid for the stock shall be augmented by the sum of $250,000 for each year by which such restoration pre-

AGE BLEED THRU

cedes 1973 (App. p. G6). As Chairman McAndless of the Price Determination Committee explained (Tr. p. 155), there might be a restoration of non-can benefits somewhat prior to 1973 and $250,000 is a rough average of the capitalized value as of 1948 of annual earnings estimated to emerge in distant years. (Ex. 28, p. 22.) Although it would have been logical to do so, the Plan makes no comparable downward adjustments of price in the event that restoration of non-can benefits should occur after 1973 but before the 1983 termination of the Plan. The Committee would have been justified in valuing the stock and fixing its price without any provisions for augmentations, and hence the $250,000 annual augmentation is a bonus or premium operating solely to Appellants' advantage, and provisions for its payment cannot be justly characterized as "grossly confiscatory" (No. 584, p. 30; No. 585, p. 27). Since the question of whether a bonus is to be paid cannot be determined until non-can benefits have been restored, it is in no sense "unfathomable" (No. 584, p. 31) but entirely logical and reasonable that no interest should be payable on the bonus until liability for its payment has been determined (Tr. pp. 327-329).

Interest Rate. The final element in the total price, which includes the value of the stock and the bonus for early restoration of non-can benefits, is interest. As fixed by the Plan, the interest rate for each year is the stated rate of the furthest maturity U. S. Government bonds outstanding at the end of the previous year (App. p. G6). The rate was 2½% until December 31, 1953, and since then has been 3¼%, based upon Treasury bonds due June 15, 1983. Since the stock was valued by the Price Determination Committee on the assumption

DARK F

that there was no risk that earnings would not emerge between 1948 and 1973 sufficient to restore non-can benefits, it is appropriate, and certainly not "confiscatory," as Appellants say (No. 584, pp. 29-30; No. 585, p. 13), that interest during the restoration period should likewise be at a no-risk rate (Ex. 28, pp. 6-7; Tr. p. 149). The provision of the Plan that interest should be paid at the time of the payment of the price of the stock rather than currently is required by the Rehabilitation Agreement, which prohibited the use of corporate earnings for other than the restoration of non-can benefits (App. p. F16). Consequently the cases cited by Appellants relating to interest (No. 584, pp. 29-30; No. 585, p. 13) have no application; they deal with a present right to a sum of money which is withheld until a later date, which is not the situation here.

Additions to Surplus. Appellants claim that the Committee's valuation is "absurd" and an "outrageous departure" because it does not take into account "the accumulating surplus as an element of value" (No. 584, pp. 27-28).

The Committee's valuation assumed that earnings of the Company would increase from year to year in the future and it valued the stock on the basis of these assumed increased earnings. It also took into account the fact that as the Company's business grew it would increase its surplus. As Chairman McAndless of the Committee testified, maintenance of an adequate surplus in relation to assets is necessary to sell insurance competitively and to permit a company to take the risks necessary to enable it to make profitable investments (Tr. pp. 282-283). The Committee calculated that $190,000 per year plus inter-

AGE BLEED THRU

est on that sum would keep the surplus in proper relationship to assets (Tr. pp. 546-547).

The Committee properly excluded this amount from the annual earnings which it capitalized in valuing the stock. This procedure simply excluded from the capitalized value of the earnings which would emerge in each year that portion which would necessarily be left in the business in order to produce the increased earnings estimated for future years—allowing, however, interest on the cumulative retained earnings which it assumed would be added to surplus (Tr. pp. 545-547). Appellants, however, would have this increase in surplus valued twice, by including in the valuation not only the earnings from such assets but also the assets themselves. Since the increase in assets is valued by capitalizing the earnings thereon, it would be a duplication to add to such valuation the amount by which the assets are increased. Bonbright says, in speaking of commercial or investment value,

> "But care must be taken not to include current assets which cannot be disposed of without impairing the earning capacity of the continuing business. Otherwise the appraiser would be guilty of double counting in capitalizing an earning power which is dependent, in part, on the retention of the very assets whose disposition he assumes." (Bonbright, Valuation of Property, Vol. I, p. 239.) See also: Finletter, Principles of Corporate Reorganization, p. 498.

Appellants' criticism ignores these sound bases for the Committee's action.

Deferred, Conditional Payment. The Plan provides that the purchase price for the stock shall not be paid until non-can benefits have been fully restored and the

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financial condition of the Company shall be such, according to standards specified in the Plan, that the Company can make the payment and leave itself in a safe financial condition.* The Conditions specified are a minimum for the safety of the policyholders (Tr. pp. 280-281). Under the Plan, the price paid to the stockholder between 1962 and 1980 will be from a high of $7,002,500 to a low of $5,325,000, depending on the year in which payment can be made.

It is settled by the decisions below, and beyond attack here, that such deferred, conditional payment was contemplated by the Rehabilitation Agreement. Appellants' attack on this feature of the Plan (No. 584, pp. 4, 25-26; No. 585, p. 48) is an attempt to repudiate the Rehabilitation Agreement. The District Court of Appeal said,

> "Various provisions of the Rehabilitation and Reinsurance Agreement show that the agreement contemplated that the price determination committee could promulgate a Plan of Mutualization and fix the price and terms of payment for the stock prior to the full restoration of non-can benefits; and that in such case payment for the stock would be postponed until after restoration of non-can benefits had been completed. Inherent in the fact that the agreement contemplated such postponement of payment, is a

*Appellants assert (No. 584, p. 15) that the provision of the Plan conditioning payment upon the safe financial condition of the Company necessarily results in the stock having, upon the basis of required surplus, a book value at the time of payment greater than that assigned to it by the Price Determination Committee. Their argument ignores the fact that the Committee properly determined the value of the stock as of 1948 (see pp. 22-23 *supra*). In addition, it illustrates the dangers of using figures from outside the record; the hypothetical surplus which they construct includes not only corporate surplus but also surplus belonging to the participating life policyholders in which the stockholders have no interest whatever.

E BLEED THRU

> further fact that the agreement contemplated that the Plan of Mutualization should not obligate New Company unconditionally to make the postponed payment." (App. p. B14.)

An even more detailed analysis of the controlling provisions of the Agreement was made by the Superior Court (App. pp. C28-C30).

Since deferred, conditional payment was contemplated by the Rehabilitation Agreement, the practicable accomplishment of mutualization did not require that the Company be capable of consummating the Plan immediately but rather that the Company be capable of putting the Plan into execution with reasonable probability of success. Appellants' contention that the Committee's finding that mutualization could "then be practicably accomplished" was "plainly contrary to the fact" (No. 585, p. 11) ignores the binding effect of the state court decision interpreting the Rehabilitation Agreement as contemplating both a deferred and a conditional payment.

* * * * *

Finally, it must not be forgotten that Appellants submitted no evidence as to the proper price of the stock or as to appropriate terms of payment. There was no evidence before the Commissioner contradicting the testimony of the experts or the detailed exhibits supporting the Plan.

Section 11527 of the Insurance Code entrusts to the Insurance Commissioner the power and duty to determine whether *"in his opinion"* a plan of mutualization protects the rights and interests of the interested parties and whether *"he is satisfied"* that the plan will be fair and equitable in its operation. As this Court has said in connection with the duties of the Securities and Exchange

Commission in considering a plan of reorganization under the Public Utility Holding Company Act, the Insurance Commissioner's conclusion here

> "rests squarely in that area where administrative judgments are entitled to the greatest amount of weight by appellate courts. It is the product of administrative experience, appreciation of the complexities of the problem, realization of the statutory policies, and responsible treatment of the uncontested facts. It is the type of judgment which administrative agencies are best equipped to make and which justifies the use of the administrative process." *Securities and Exchange Commission v. Chenery Corp.*, 332 U. S. 194, 209.

In such cases the administrative officer's conclusion will be disturbed "only if it lacks any rational and statutory foundation" *Id.* at 207.

C. The Proceedings Below Met Every Requirement of Procedural Due Process.

Trial de novo. Appellants claim that they were entitled to an independent judicial review—a trial *de novo*—of the Commissioner's approval because it was attacked as confiscatory (No. 584, pp. 37-38; No. 585, pp. 44-45). The court below held that under California law "The function of the superior court was to determine whether the action taken by the Commissioner was arbitrary or constituted an abuse of discretion" and that it properly refused to conduct a trial *de novo* (App. p. A14). This construction of the California law is not open to challenge in this Court. *Neblett v. Carpenter*, 305 U. S. 297, 302.

The Fourteenth Amendment requires no more. Recent decisions of this Court establish that courts need

AGE BLEED THRU

not conduct a trial *de novo* in reviewing the action of administrative agencies. *Alabama Public Service Commission v. Southern Ry. Co.,* 341 U. S. 341, 349; *Railroad Commission of Texas v. Rowan & Nichols Oil Co.,* 311 U. S. 570, 576. Moreover, this Court has expressly sanctioned the "substantial evidence" rule as applied to judicial review of administrative determinations of value. *Securities and Exchange Commission v. Central Illinois Securities Corp.,* 338 U. S. 96, 126 (1949); *Ecker v. Western Pacific R. Corp.,* 318 U. S. 448, 477.

These cases show that the *Ben Avon* and *St. Joseph Stockyards* cases, upon which appellants base their argument (No. 584, pp. 37-38), have been limited to their special facts and do not require a trial *de novo* whenever action by a state agency is attacked as confiscatory. In *American Trucking Assn. v. United States,* 344 U. S. 298, 321, this Court emphasized that " 'Confiscatory' is not a magic word" and that the "claim of rate confiscation" stands on a "fundamentally different footing."

In the *Trucking Assn.* case, this Court held that the appellants there were not entitled to a hearing *de novo* because they had been afforded an opportunity to present evidence before the Commission and because of the nature of the order under attack. 344 U. S. at pp. 320-322. In the present case, Appellants had ample opportunity to present evidence to the Commissioner. Indeed in the Superior Court, Appellants were offered, but declined, an opportunity to make a showing which would warrant the remand of the case to the Insurance Commissioner for

DARK P

the taking of additional evidence as permitted by Section 1094.5 of the Code of Civil Procedure (Clk. Tr. pp. 220, 236). Moreover, as we have pointed out, the administrative action involved here is not an order, but merely an action approving the Plan by which the Company might purchase its own stock. In these circumstances, the Fourteenth Amendment does not require that California afford Appellants a trial *de novo.*

Alleged Conflict of Interests. The charge by Appellants (No. 584, p. 39) that the Commissioner was involved in a "hopeless conflict of interests" requires only brief mention. The argument is that the Commissioner could not properly discharge his duties under Section 11527 of the California Insurance Code because, as Liquidator, he was bound to consent to the Plan. This circumstance, however, was contemplated by the Rehabilitation Agreement itself. Moreover, the fact that consent had been given by one Commissioner in 1936 did not mean that the mind of another Commissioner in 1950 was "irrevocably closed on the subject," or that the latter Commissioner would not conscientiously perform his statutory duty. See *Federal Trade Commission v. Cement Institute,* 333 U. S. 683, 701. Furthermore, since the Commissioner's approval is essential to mutualization, the rule of necessity would enable him to act even had there been a real conflict of interest. *Evans v. Gore,* 253 U. S. 245, 247-248; *Brinkley v. Hassig,* 83 F. 2d 351, 357 (10th Cir. 1936).

GE BLEED THRU

III.

There Is No Important or Recurrent Question of Federal Law Involved.

Appellants here challenge the California Insurance Commissioner's approval of a unique and necessarily complex Plan of Mutualization. It is highly unlikely, in view of the special circumstances of the Plan, that a similar question will ever occur again. Enough has been said above to show that the questions here cannot have significance beyond the particular facts and parties involved. The claims of Appellants that substantial sums of money may be involved will not suffice. Review in this Court is not warranted where, as here, the problem does not reach beyond the "episodic." *Rice v. Sioux City Memorial Park Cemetery, Inc.*, 349 U. S. 70, 74.

Conclusion.

For the above reasons Appellee Pacific Mutual Life Insurance Company submits that the Appeal herein should be dismissed. If the papers on appeal are to be treated as petitions for certiorari pursuant to 28 U. S. C., Section 2103, certiorari should be denied.

Respectfully submitted,

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January, 1956.



SUBJECT INDEX

PAGE

Preliminary statement 2

Summary of argument 3

1. Appellate jurisdiction 3
2. There was no deprivation of property 3
3. California is not constitutionally required to examine the wisdom of contracts and to relieve a contracting party of a contract of which he repents 4
4. There was ample evidence to sustain the determination that the mutualization price was fair 4
5. There was no improper dual interest 5

Statement of facts 5

Seizure of Old Company 7

Rehabilitation Agreement: Generally 8

Rehabilitation Agreement: Provisions for mutualization 8

Rehabilitation Agreement: Adoption and approval 10

Validity of mutualization provisions of Rehabilitation Agreement 11

The "rights and interests" of the stockholder of New Company 12

Initiation of mutualization 12

Terms of Mutualization Plan 14

Proceedings for mutualization 15

Proceedings before the Commissioner 15

The Commissioner's decision 17

Court proceedings 18

PAGE

Argument 19

I.

The case is not within the appellate jurisdiction of this court.... 19

A. The constitutionality of the California Insurance Code Sections were not "drawn in question"..... 19

B. The decision of the Insurance Commissioner was not legislative in character..... 19

II.

The effect of the Commissioner's action is a matter of state law. As the state courts have determined, it deprives no one of property..... 21

III.

There is no constitutional requirement that the State afford a contracting party escape from a contract of which he repents 23

IV.

There was ample evidence that the price fixed was adequate.... 25

Conclusion to Part IV..... 30

V.

There was no denial of procedural due process..... 30

A. Due process does not require court review of administrative findings of fact reached after a full hearing..... 31

B. There was no improper dual position; and in any event the rule of necessity would prevent disqualification of the Commissioner 31

Conclusion 32

DARK P

TABLE OF AUTHORITIES CITED

CASES	PAGE
Alabama Commission v. Southern R. Co., 341 U. S. 341	31
American Fed. of Grain Millers v. General Mills, Inc., 117 Fed. Supp. 340	24
Atlantic Pacific Oil Co. v. Gas Dev. Co., 105 Mont. 1	24
Bank of Italy v. Johnson, 200 Cal. 1	20
California etc. Confs. of M. E. Churches v. Seitz, 74 Cal. 287	11
Caminetti v. Guaranty Union L. Ins. Co., 22 Cal. 2d 759	6
Carpenter v. Pacific Mutual, 10 Cal. 2d 307	7, 8, 11, 32
Caminetti v. Pacific Mutual, 22 Cal. 2d 344	6
Carpenter v. Pacific Mutual, 13 Cal. 2d 306	7, 32
Charleston Assn. v. Alderson, 324 U. S. 182	19
City & County of San Francisco v. Itsell, 133 U. S. 65	23
Doty v. Love, 295 U. S. 64	25
Evans v. Gore, 253 U. S. 245	31
Federal Const. Co. v. Curd, 179 Cal. 489	31
Federal Trade Commission v. Cement Inst. 333 U. S. 683	31
Galveston v. Texas, 210 U. S. 217	28
Glenn v. Bacon, 86 Cal. App. 58	11
Hamilton v. University of California, 293 U. S. 245	19
Heim v. McCall, 239 U. S. 175	21
Jett Bros. Distilling Co. v. City of Carrollton, 252 U. S. 1	19
Neblett v. Carpenter, 305 U. S. 297	7, 11, 21
Neblett v. Pacific Mutual, 22 Cal. 2d 393	2, 32
Nesseth v. Creedon, 80 Fed. Supp. 269	24
Old Dearborn Co. v. Seagram Corp., 299 U. S. 183	22
Phelps v. Harris, 101 U. S. 370	11
Relfe v. Rundle, 103 U. S. 22	6
Rosenbaum Grain Corp., In re, 83 F. 2d 391	11
Ross v. Freeman (1935), 2 Del. Ch. 44	11
Transportation Bldg. Co. v. Dougherty, 74 Cal. App. 2d 604	24

GE BLEED THRU

STATUTES **PAGE**

California Insurance Code, Sec. 1043 10
California Insurance Code, Sec. 11525 ..... 3, 19
California Insurance Code, Sec. 11526 ..... 3, 19
California Insurance Code, Sec. 11527 ..... 3, 6, 17, 19
California Insurance Code, Sec. 11529.5 15
United States Code, Title 28, Sec. 1257(2) 19

TEXTBOOKS

James, Options (1916), Sec. 1212, p. 563 11
Restatement of Law of Trusts, Sec. 190, Comment k 11
2 Scott, Trusts (1939), Sec. 190.8, p. 1034 11

DARK P

IN THE

Supreme Court of the United States

OCTOBER TERM, 1955.

No. 584

FRANK GENTLES, *et al.*,

Appellants,

vs.

F. BRITTON McCONNELL, as Insurance Commissioner of the State of California, *et al.*,

Appellees.

No. 585

THE PACIFIC MUTUAL LIFE INSURANCE COMPANY OF CALIFORNIA, *et al.*,

Appellants,

vs.

F. BRITTON McCONNELL, as Insurance Commissioner of the State of California, *et al.*,

Appellees.

On Appeal From the Supreme Court of the State of California.

MOTION TO DISMISS APPEAL.

Appellee, F. Britton McConnell, as Insurance Commissioner of the State of California, and F. Britton McConnell, Insurance Commissioner of the State of California, as Liquidator of The Pacific Mutual Life Insurance Company of California, moves the court to dismiss the appeal herein on the following grounds:

1. The appeal is not within the appellate jurisdiction of this court, since the validity of no statute is drawn in question.

GE BLEED THRU

2. The appeal does not present a substantial federal question.

3. The judgment rests on an adequate non-federal basis.

Preliminary Statement.

F. Britton McConnell, the moving party, appears here in his official position as Insurance Commissioner of the State of California. References to the "Commissioner" or the "Liquidator" herein will usually refer, not to him personally, but to one of his predecessors.

Indeed, Commissioner McConnell is the seventh Insurance Commissioner to act as Liquidator of Old Company in a period of nearly twenty years: Commissioner Carpenter entered into the Rehabilitation Agreement hereinafter discussed; he was followed in office by Commissioner Goodcell and he by Commissioner Caminetti, during whose term the Rehabilitation Agreement was again reviewed and upheld (*Neblett v. Pacific Mutual* (1943), 22 Cal. 2d 393). Then followed Commissioner Garrison and then Commissioner Downey, whose approval of the Mutualization Plan is here under review. The proceedings in the State Courts upholding that decision were conducted by Commissioner Maloney. Commissioner McConnell (the present Appellee) assumed office shortly before the decision of the California Supreme Court here under review, and was duly substituted as a party in the proceeding.

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Summary of Argument.

1. Appellate Jurisdiction.

Appellants did not raise in any of the state courts any question as to the constitutionality of the mutualization statutes (Cal. Ins. Code, secs. 11525-7), either absolutely or as construed and applied.

The Insurance Commissioner's "opinion and decision" is not legislative in character; and, although it was broadly attacked below as violative of due process, appellants have not heretofore treated it as legislative in character.

2. There Was No Deprivation of Property.

Although Appellants assert that the approval of the Commissioner "binds" them to a sale of stock, the decision of the California Court is explicit that

> "The approval of the mutualization plan by the Commissioner did not involve any deprivation of property rights or vested rights; it was in essence a permit or license authorizing the new company to purchase its own stock." [Juris. St. (Co.) Appx. p. 13a; Juris. St. (Gentles) Appx. p. A-14.]

The stockholder of New Company (*i.e.*, the Liquidator, in whose right appellants sue) is left free by the Commissioner's approval to sell or not as he sees fit, except as the contract of his predecessor, made in 1936 and not here under review, is enforceable against him.

Appellants' real complaint is that the Liquidator proposes to carry out that contract; but his making of the contract was approved by the California courts in 1936, in a proceeding to which appellants (or their predecessors) were parties, and which has been final for nearly a score of years.

GE BLEED THRU

3. California Is Not Constitutionally Required to Examine the Wisdom of Contracts and to Relieve a Contracting Party of a Contract of Which He Repents.

Appellants complain that the California courts "wrote out of Sec. 11527 of the Insurance Code" a (supposed) requirement that the Commissioner withhold approval unless it appears that the price to be paid thereunder is one which would provide the equivalent of full compensation under an eminent domain statute. [Juris. St. (Gentles) p. 20. See also Juris. St. (Co.) p. 43, *et seq.*]

Since the decision is one of the highest State court (and is accordingly the authoritative interpretation of the statute) it is doubtless more accurate to say that the State Legislature has not seen fit to prohibit a stockholder from voluntarily disposing of his stock merely because he is not receiving a fully compensatory price.

Our attention has not been called to any authority (and we know of none) suggesting that California is constitutionally required so to interfere with the freedom of contract.

4. There Was Ample Evidence to Sustain the Determination That the Mutualization Price Was Fair.

Despite the fact that, under the statute as construed by the California courts, the Commissioner was not required to determine the adequacy of the price the stockholder had agreed to take, he did receive lengthy testimony from highly competent experts, which fully sustained his decision. The new Company was earning less than $1,000,000 a year; and the holders of non-can policies had a prior claim to those earnings in the amount of some $22,000,000 (plus interest). The determination of the experts that the value of the stock did not exceed $3,000,-

DARK P

000 under those circumstances is not surprising; and the attempts of Appellants to reinterpret the data on which the experts relied are misleading and unconvincing.

5. There Was No Improper Dual Interest.

As the California Supreme Court points out [Juris. St. (Co.) Appx. p. 6a; Juris. Ct. (Gentles) Appx. p. A7], the fact that Commissioner Carpenter, as Conservator, in 1936 consented to such plan of mutualization as a committee might submit, could scarcely disqualify Commissioner Downey from passing on the fairness of the plan as submitted in 1950. Moreover, as has frequently been held, disqualification will not be permitted to destroy the statutory scheme by removing the one officer whose duty it is to act.

Statement of Facts.

The Company being mutualized is Pacific Mutual Life Insurance Company—"New Company."

Appellants are not stockholders of New Company, and have no direct interest in it. Old Company has a residual interest, somewhat akin to a bankrupt's interest in property held by a trustee in bankruptcy; and the other appellants' interest is that of stockholders of Old Company.

The sole stockholder of New Company is the Insurance Commissioner of the State of California, acting as Liquidator under the California statutes[1] (or, more accurately,

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[1]The Insurance Commissioner is made a party to these proceedings in two capacities. *One:* in his administrative capacity as a State Officer he (*i. e.*, Commissioner Downey, in 1950) approved the plan of mutualization; and the proceedings below sought to compel him to reverse the ruling. When we have reference to him primarily in that capacity, we shall refer to him as "Commissioner." *Two:* he is and he and his predecessors (commencing

GE BLEED THRU

legal title is in certain Voting Trustees to whom the stock was transferred as permitted by California law: *Caminetti v. Pacific Mutual* (1943), 22 Cal. 2d 344). He acquired his title as the "statutory successor" to Old Company. (*Caminetti v. Guaranty Union L. Ins. Co.* (1943), 22 Cal. 2d 759, 763-4; see also *Relfe v. Rundle* (1881), 103 U. S. 22, 225.)

Accordingly, it is the Liquidator whose rights are affected by the proposed mutualization. Appellants therefore made demand on him to bring the mandamus proceeding; and upon his refusal, instituted it themselves as a derivative action.[2] [Clk. Tr. 4, see also Juris. St. (Co.), p. 45, note 23.]

Since the Commissioner, before approving the plan, was required by statute to determine whether, in his opinion, the rights and interests of the shareholder were protected by the plan,[3] it is necessary to examine the background to see what the "rights" of the shareholder (and of appellants) were.

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with Commissioner Carpenter in 1936) have been, the "statutory successor" of Old Company (as Conservator from mid-1936 to February 1937; as Liquidator thereafter), and as such he became the owner of all of the stock of New Company. When we have reference to him primarily in that capacity, we shall refer to him as "Liquidator."

[2]The California District Court of Appeal referred to this situation in saying that the evidence was not insufficient to justify the Commissioner's conclusion that the mutualization plan protected the rights of "all interested parties, including the stockholder, *in whose right the appellants sue.*" [Juris. St. (Co.) Appx. p. 81a; Juris. Statement (Gentle) Appx. p. B-23].

Note: There are two Jurisdictional Statements on file—one on behalf of Old Company and two individuals; the other on behalf of four individuals. We distinguish the two Statements as above.

[3]Calif. Ins. Code, sec. 11527; Juris. St. (Co.) Appx. p. 169a-170a; Juris. St. (Gentles) Appx. p. E-11-12.

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Seizure of Old Company.

In 1936 the then Insurance Commissioner found Old Company to be insolvent;[4] and, acting under the statutory procedure provided by California, took over its assets as Conservator (later Liquidator). Although initial orders made in the court proceeding were void,[5] they were followed some three weeks later by a valid order.[6] (See *Carpenter v. Pac. Mutual* (1937), 10 Cal. 2d 307, *324,* affd. *Neblett v. Carpenter* (1938), 305 U. S. 297, *301.*)

Since 1936 the assets theretofore owned by Old Company have been vested in the Conservator-Liquidator. Since 1936 neither the Old Company nor its stockholders,[7] has had the right to determine when such assets shall be sold and for how much. If that is the deprivation of property of which appellants complain, their appeal is from the wrong order, and is nearly twenty years too late.

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[4]Whether there was an insolvency in the "bankruptcy or equity senses of the term" [See Juris. St. (Co.) p. 6], or whether its difficulties were "of a temporary character" [Juris. St. (Gentles) p. 6, note: Juris. St. (Co.) p. 18] is here immaterial. That action is not under attack. However, it may be noted that its liabilities exceeded its assets by at least $17,000,000; and today, after nearly 20 years, the New Company has not yet been able to make up the deficits.

[5]The orders were found to be void when it was found that the judge who made them was a policyholder in Old Company. [*Cf.* Juris. St. (Co.) p. 7, p. 29.] Two Justices of the California Supreme Court disqualified themselves for the same reason in 1937, and one did so in the instant proceeding. One Justice of the Supreme Court of the United States similarly disqualified himself in 1938.

[6]Old Company is in error in asserting that this order was made *ex parte* [Juris. St. (Co.) p. 7.] (See *Carpenter v. Pac. Mutual* (1938), 13 Cal. 2d 306, 316.)

[7]As suggested by Juris. St. (Gentle) p. 26.

GE BLEED THRU

Rehabilitation Agreement: Generally.

The Conservator dealt with the problem before him by organizing New Company, and by transferring to it substantially all of the assets formerly owned by Old Company pursuant to a Rehabilitation Agreement under which New Company assumed the obligations of Old Company *except* those arising under certain "Non-Can" policies. The latter were only partially asumed, but New Company agreed to use all of its funds available for general corporate purposes, and not reasonably required for its operations, for the restoration of the full benefits under those policies. [Juris. St. (Gentles), p. F-16, *et seq.*]

The first essential in the scheme of rehabilitation was, accordingly, that New Company be set up in such a manner that it could operate successfully and profitably in competition with other insurance companies. (See discussion in *Carpenter v. Pac. Mutual* (1937), 10 Cal. 2d 307, 336-7.) Most of the provisions of the Rehabilitation Agreement were directed to that end.

Rehabilitation Agreement: Provisions for Mutualization.

As the State Supreme Court observes, "The Commissioner apparently concluded that a plan for mutualization which could not be destroyed by future action or nonaction of the shareholders was necessary as a means of inducing both former and prospective policyholders to deal with the new company and thus permit its continued existence." [Juris. St. (Co.), Appx. p. 12a; Juris. St. (Gentles), Appx. p. A-13.]

Accordingly, the Rehabilitation Agreement contained what is described as an "option to mutualize." [See

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Juris. St. (Co.), Appx. pp. 149a, 150a, 151a; Juris. St. (Gentles), Appx. pp. F-28-30.]

The option is spelled out in the Agreement in considerable detail [Rehab. Agmt. Art. 20; Juris. St. (Gentles), Appx. p. F-24 *et seq.;* Juris. St. (Co.), Appx. pp. 146a-152a].

The option is exercisable by the holders of Participating Life Insurance policies. In should be observed that they paid handsomely for their option: $4,792,118.77 was transferred from the surplus of the Participating Life Department of Old Company to the general funds of New Company, and 10% of the profits of the participating life policies written by Old Company [amounting to more than $2,000,000; Ex. 28, p. 13-A] has been similarly transferred [Rehab. Agmt. Art. 6, Juris. St. (Gentles), Appx. pp. F-6-10]. The participating policyholders had a claim to these funds prior to the claims of stockholders. [Juris. St. (Co.), Appx. p. 68a; Juris. St. (Gentles), Appx. pp. B-7-8.]

On the written request of 10% of the holders of participating life policies, made after the expiration of ten years, an Appointing Committee consisting of the President of the Life Insurance Association of America,[8] the President of Stanford University, and the Provost of the University of California at Los Angeles would be established.

That Committee would appoint not less than three nor more than five persons "skilled in insurance company valuation" to determine whether mutualization was "then prac-

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[8]Formerly known as the "Association of Life Insurance Presidents."

AGE BLEED THRU

ticable"; and, if so, to determine the "proper price" to be paid on mutualization, to fix the time and terms of payment, and to prepare a plan of mutualization, which might include a voting trust, with provisions for successor trustees.

New Company expressly agreed that if 10% of the participating life policyholders so requested it would submit the plan in accordance with California law. The Conservator, for himself and his successors in interest, "agrees to consent and hereby consents, as the holder and owner of the stock of New Company, to such plan of mutualization."

And further, "In the event said plan of mutualization is adopted, the Conservator, or a Liquidator as aforesaid, shall dispose of said stock in accordance with such plan." [Juris. St. (Gentles) Appx. p. F-27; Juris. St. (Co.) Appx. p. 148a.]

Rehabilitation Agreement: Adoption and Approval.

Before executing the Rehabilitation Agreement, the Conservator [in accordance with California law: Cal. Ins. Code, Sec. 1043, Juris. St. (Co.) Appx. p. 177a; Juris. St. (Gentles) Appx. p. B-1] submitted it to the appropriate court for approval.

Old Company was a party to that proceeding; and representative appearances were made by many of its stockholders. [Recitals, Ex. 8.]

The California court approved the Rehabilitation Agreement and its execution; and authorized the Liquidator "without further order of this court, fully and faithfully to perform, carry out, and discharge" its terms. [Ex. 8, par. 15.]

DARK PAGE

The Supreme Court of California (*Carpenter v. Pacific Mutual* (1937), 10 Cal. 2d 307), and this Court, on certiorari, (*Neblett v. Carpenter* (1938), 305 U. S. 297) affirmed.

Validity of Mutualization Provisions of Rehabilitation Agreement.

The Supreme Court of California held—as a matter of California law—that

> ". . . the stockholders of a solvent company can contract to consent to a future plan of voluntary mutualization (*Cf.* Market St. Ry. Co. v. Hellman, 109 Cal. 571, 586-7)[9] and no sound reason appears why such an agreement is improper merely because the shares are held by the commissioner as conservator of a seized insurer[10] . . . The powers vested in the commissioner by sections 1037 and 1043[11] are sufficiently broad to authorize him, as sole stockholder, to give advance consent to the plan of mutualization. Moreover, the validity of all portions of the rehabilitation agreement, including the provision for advance consent, is *res judicata.*" [Juris. St. (Co.) Appx. p. 12a; Juris. St. (Gentles) Appx. p. A-13.]

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[9]The Court might have added that options and contracts at a price to be fixed by valuers are commonplace in California and elsewhere: James, Options (1916), Sec. 1212, p. 563; *Glenn v. Bacon* (1927), 86 Cal. App. 58, 69; *Calif. etc. Confs. of M. E. Churches v. Seitz* (1887), 74 Cal. 287; and authorities cited by California District Court of Appeal, Juris. St. (Co.) Appx. p. 90a; Juris. St. (Gentles) Appx. p. B-32.

[10]Again the Court might have added that such contracts made by fiduciaries are not uncommon. *Ross v. Freeman* (1935), 2 Del. Ch. 44; *Phelps v. Harris* (1880), 101 U. S. 370, 383; *Re Rosenbaum Grain Corp.* (1936; C. C. A. 7th), 83 F. 2d 391, 394; 2 Scott, Trusts (1939), Sec. 190.8, p. 1034; Restatement Trusts, Sec. 190 comm. k.

[11]Of the California Insurance Code.

The "Rights and Interests" of the Stockholder of New Company.

In the words of the California District Court of Appeal:

> "The result of Judge Willis' order of December 4, 1936, was that . . . the conservator acquired valid title to all of the capital stock of New Company, subject, however, to an option to the participating life policyholders of New Company, through mutualization proceedings initiated after approximately 10 years, to cause New Company to acquire such stock at the price and on the terms fixed by a duly appointed price determination committee, in the event that such committee should determine that in its opinion mutualization was practicable." [Juris. St. (Co.) Appx. p. 74a; Juris. St. (Gentles) Appx. p. B-14.]

Initiation of Mutualization.

In 1946, on the written request of more than 10% of the participating life policyholders [Exs. 10, 11] the Appointing Committee[12] was created. That Committee appointed the Price Determination Committee, consisting of Alva J. McAndless, President of Lincoln National Life Insurance Company, a stock company and the tenth largest life insurance company in the United States; Ray D. Murphy, Vice President and Chief Actuary of The Equitable Life Insurance Company of the United States, one of the five largest in the country; Horace R. Bassford, Vice President and Chief Actuary of Metropolitan Life Insurance Company, the largest life insurance com-

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[12]George Willard Smith, President of the Life Insurance Association of America; Dr. Donald B. Tressider, President of Stanford; and Dr. Clarence A. Dykstra, Provost of the University of California at Los Angeles.

DARK PAGE

pany in the country; and Albert J. Hettinger, a partner in the well-known investment banking firm of Lazard Freres and Company and former professor of Business Economics in the Harvard Graduate School of Business Administration.[13]

Broad executive experience (Mr. McAndless); practical investment experience (Mr. Hettinger); a professor's theoretical knowledge of economic theory, coupled with its practical application in the Federal Reserve system (Mr. Hettinger); and the actuary's training in the practical measurement and evaluation of future contingencies (Messrs. Bassford, and Murphy, as well as McAndless), were combined to furnish what was doubtless the most able and well-balanced group ever to study any comparable problem.

The Committee made what Mr. McAndless characterized as "one of the most complete investigations of earning power that has ever been made for any life insurance company." [Tr. p. 134, line 1.] It occupied a period of some three years, and approximately 10,000 man-hours of work were expended by the staff. [Tr. p. 135, line 25.]

The Committee determined that mutualization was then practicable;[14] and prepared the Plan of Mutualization here in controversy. [Juris. St. (Co.) Appx. pp. 152a, *et seq.;* Juris. St. (Gentles) Appx. G.]

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[13]A further summary of the background and experience of the committee members appears in the opinion of the District Court of Appeal [Juris. St. (Co.) Appx. pp. 75a-77a; Juris. St. (Gentles) Appx. p. B16-18.]

[14]Appellants Gentles *et al.* suggest that this determination is at odds with the provisions for deferred payment. [Juris. St. (Gentles) p. 104.] The trial court pointed out that the Rehabilitation Agreement contemplated deferred payments; and that the requirement of a determination that mutualization was "then practicable"

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Terms of Mutualization Plan.

The plan fixes the purchase price of the stock at $3,000,000, with interest at Government Bond rates; but with a provision that if restoration of Non-Can benefits is accomplished prior to 1973, the price shall be increased by $250,000 for each full year by which such restoration antedates that date.

"For the purpose of accumulating a fund to be used in payment, at least in part" of the purchase price, the Company is directed to set aside in a separate fund 5% of the profits of the Participating Department (excluding profits allocable to policies issued by Old Company).[15]

Payment is to be made when three conditions shall all have been met:

1. Restoration of Non-Can benefits is completed.

2. The Special Fund, plus the amount of capital and corporate surplus equals or exceeds the purchase price.

3. The admitted assets of New Company, after paying for the shares, will exceed its liabilities by 4% of its assets, plus 25% of the preceding years premium on one year term Group policies, and on all of its Accident and Health insurance.

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related to the fact that in 1936, before operations under the Rehabilitation Agreement had commenced, it was impossible to make any predictions on which a valuation of the enterprise could be based. [Juris. St. (Co.) Appx. p. 118a-119a; Juris. St. (Gentles) Appx. p. C-28.] This interpretation of the agreement has now been conclusively adopted by the appellate courts of California.

[15]It will be recalled that under the Rehabilitation Agreement, the profits of the Participating Department are not available for general corporate purposes, but belong to the policyholders of that Department as if it were a separate mutual insurance company. [Ex. 9, Par. 6; Juris. St. (Gentles) Appx. pp. F-6-10.]

DARK PAG

If the purchase price is not paid on or before December 31, 1983, the plan shall be considered to have failed, and shall terminate.

Pending payment of the purchase price, a new voting trust is set up. This procedure was expressly contemplated by the Rehabilitation Agreement [Ex. 9, par. 20(a); Juris. St. (Co.) Appx. p. 148a; Juris. St. (Gentles) Appx. p. F-26]; and is expressly permitted by statute. [Ins. Code, Sec. 11529.5; Juris. St. (Co.) Appx. p. 173a.]

Proceedings for Mutualization.

More than 10% of the participating life policyholders having requested the submission of the plan,[16] New Company, in accordance with its agreement in the Rehabilitation Agreement and with the applicable statute, adopted the Plan. It was adopted by the board of directors, and the approval of the shareholders had been given in the Rehabilitation Agreement. The California Supreme Court has authoritatively determined that this adoption and approval complied with state law.[17]

Proceedings Before the Commissioner.

At the hearing before the Commissioner, Mr. McAndless and Mr. Hettinger were qualified as experts and

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[16]Old Company asserts that the life policyholders have not appeared in this proceeding [Juris. St. (Co.) p. 31, Note 17], and suggests a lack of interest on their part. However, they have twice requested mutualization; and more than 40,000 of them made request for the submission of this particular plan. [See recital, Ex. 19.]

[17]Juris. St. (Co.) Appx. pp. 11a-12a; Juris. St. (Gentles) Appx. pp. A12-A14. In addition to the consent in the Rehabilitation Agreement, the Voting Trustees executed a formal approval. [Exs. 21, 22.] See opinion of District Court of Appeal, Juris. St. (Co.) Appx. pp. 89a-90a; Juris. St. (Gentles) Appx. pp. B-31-2.

BLEED THRU

testified at length. Their ultimate conclusion was that the value of the stock of New Company was $2,500,000. [Tr. pp. 153-4; Tr. pp. 396-7.] To this amount the Committee had added $500,000 under a requirement of the Rehabilitation Agreement that certain participating insurance should be treated as non-participating for the purpose of fixing the mutualization price. [Juris. St. (Co.) Appx. p. 147a; Juris. St. (Gentles) Appx. p. F-26.]

The witnesses did not content themselves with stating their ultimate conclusion. They testified at length as to their reasons, and introduced [Ex. 28] a volume containing their major data.

They pointed out that "by the processes ordinarily employed in the evaluation of an enterprise, the stockholders' interest would be considered valueless or of negligible value." [Ex. 28, p. 23.] That is, the $22,000,000 prior claims of the Non-Can policies would exhaust any value that would ordinarily be placed on a company earning less than $1,000,000 a year, or with the business in force, or the capital and surplus, of New Company.

However, by attempting to forecast a "pattern" of future profits—increasing from some $872,000 a year in 1949 to some $3,351,000 a year in 2000 A. D.; and capitalizing those estimated profits, they arrived at a figure ($2,600,000) consistent, when adjusted, with their estimated value of $2,500,000.

No evidence was offered to the contrary.

The Commissioner's Decision.

The California statute provides that the Commissioner shall not approve a plan of mutualization "unless in his opinion the rights and interests of the insurer, its policyholders and shareholders are protected, and unless he is satisfied that the plan will be fair and equitable in its operation. [Cal. Ins. Code, Sec. 11527; Juris. St. (Co.) Appx. pp. 169a-170a; Juris. St. (Gentles) Appx. pp. E-11-12.]

As authoritatively construed by the California courts,

> "The basic problem for the Commissioner to determine was whether or not the price and terms of payment for the New Company stock were fixed in accordance with the rehabilitation agreement, for if they were, the Plan of Mutualization is fair and equitable because it gives the stockholder the price and terms he agreed to take." [District Court of Appeal; Juris. St. (Co.) Appx. p. 91a; Juris. St. (Gentles) Appx. pp. B-33-4.]

However, the Commissioner did not rest there. He considered the testimony of the members of the Committee—the only evidence before him—and concluded that "there was abundant evidence to support the findings of the committee as to the price of three million dollars, both upon the basis of a price to be paid for non-participating life insurance in force, and upon other bases." [Juris. St. (Co.) Appx. p. 141a; Juris. St. (Gentles) Appx. p. D-17.]

His "Opinion and Decision" concludes with his finding, in the words of the statute; and with his conclusion that the plan is lawful and meets the requirements of the Code.

The operative decision is simply "The plan is therefore hereby approved." [Juris. St. (Co.) Appx. p. 145a; Juris. St. (Gentles) Appx. p. D-22.]

As we have pointed out, and as the California courts have held, it does not "order" anything, or compel anything.

Court Proceedings.

The trial court, the District Court of Appeal [See particularly Juris. St. (Co.) Appx. pp. 81a-83a; Juris. St. (Gentles) Appx. pp. B-22-5], and the Supreme Court [See Juris. St. (Co.) Appx. pp. 13a-14a; Juris. St. (Gentles) Appx. p. A-15] have all held that there was adequate evidence to support the findings of the Commissioner.

DARK PAGE

ARGUMENT.

I.

The Case Is Not Within the Appellate Jurisdiction of This Court.

A. The Constitutionality of the California Insurance Code Sections Were Not "Drawn in Question."

Appellants do not point out, nor have we found, any place in these proceedings prior to their notice of appeal to this Court at which they have asserted the unconstitutionality of California Insurance Code sections 11525-7, either of themselves or as applied.

Such challenge comes too late.

Charleston Assn. v. Alderson (1945), 324 U. S. 182, 185;

Jett Bros. Distilling Co. v. City of Carrollton (1920), 252 U. S. 1, 6.

B. The Decision of the Insurance Commissioner Was Not Legislative in Character.

Appellants urge that an "order" of a state administrative body may be legislative in character, and hence a "statute" within the meaning of 28 U. S. C., Sec. 1257(2).

Of course, that term "is used to include every act legislative in character to which the state gives sanction . . ." (*Hamilton v. University of California* (1934), 293 U. S. 245, 258).

But it is clear here that California gives no "sanction" to the Commissioner's approval; the State courts have expressly held that it is a mere permit or license [Juris.

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St. (Co.) Appx. p. 13a; Juris. St. (Gentles) Appx. p. A-14], and "did not compel the life policyholders to approve the plan, nor the stockholder to dispose of the stock as therein provided, or the New Company to adopt the plan." [Juris. St. (Co.) Appx. pp. 91a-92a; Juris. St. (Gentles) Appx. p. B-34.]

Nor was the Commissioner's action legislative in character—as Appellants themselves observed in the State courts:

> "The Commissioner was not conducting hearings in the legislative field; he did not issue an order setting forth rules of future conduct for an entire industry or type of business." (Pet. for Reh., Dist. Ct. of A., p. 58; See also Pet. for Hearing, Sup. Ct., p. 60.)

On the contrary, as Appellants stated to the State Supreme Court:

> "If the question before the board or officer is whether a particular person should be granted a license or permit to engage in a particular business or profession, then the board or officer is generally considered to be acting in an administrative or executive capacity." (Pet. for Hearing, Sup. Ct., p. 61.)

Accord: *Bank of Italy v. Johnson* (1926), 200 Cal. 1, 13, 16.

It is quite apparent from the foregoing that the State court was not told it was being asked to determine the constitutionality of a "statute of the state"—that such matter was not "drawn in question."

II.

The Effect of the Commissioner's Action Is a Matter of State Law. As the State Courts Have Determined, It Deprives No One of Property.

Appellants repeatedly claim that the Commissioner's approval "binds them" to a sale of the stock. [*e. g.*, Juris. St. (Co.) pp. 4, 43; Juris. St. (Gentles) p. 3.]

But the California courts have explicity held to the contrary.

The California Supreme Court says:

> "The approval of the mutualization plan by the commissioner did not involve any deprivation of property or vested rights; it was in effect a permit or license authorizing the new company to purchase its own stock." [Juris. St. (Co.) Appx. p. 13a; Juris. St. (Gentles) Appx. p. A-14.]

The District Court of Appeal says:

> "On this question of due process we should never lose sight of the fact that the commissioner's approval of the Plan of Mutualization did not have the effect of taking appellants' property, since it was nothing more or less than a permit, and did not compel the life policyholders to approve the plan, nor the stockholder to dispose of the stock as therein provided, or the New Company to adopt the plan." [Juris. St. (Co.) Appx. pp. 91a, 92a; Juris. St. (Gentles) Appx. B-34.]

The question of the meaning and application of the state statutes is manifestly one of state law.

Heim v. McCall (1915), 239 U. S. 175, 189;

Neblett v. Carpenter (1938), 305 U. S. 297, 302.

Indeed, Appellants seem to agree as to the effect of the approval. [See Juris. St. (Co.) p. 9; Juris. St. (Gentles) p. 36.]

The stockholder (*i. e.*, the Liquidator, in whose right Appellants sue) is manifestly not unconstitutionally deprived of property when his property may be taken only as he voluntarily chooses to dispose of it by contract.

To borrow a dictum of this Court:

> "It (a Fair Trade statute) *permits*[18] the designated private persons to contract with respect thereto. It contains no element of compulsion, but simply legalizes their acts, leaving them free to enter into the authorized contract or not as they see fit. Thus far the act is plainly not open to objection; and none seems to be made."
>
> *Old Dearborn Co. v. Seagram Corp.* (1936), 299 U. S. 183, 192.

As the District Court of Appeal observes,

> "The compulsion upon the stockholder flows from the obligations of the Rehabilitation and Reinsurance Agreement, and not from the commissioner's approval of the plan." [Juris. St. (Co.) Appx. p. 92a; Juris. St. (Gentles) Appx. pp. B-34-5.]

If the covenant in the Rehabilitation Agreement had been invalid (as Appellants sought to urge below), the Liquidator would be entirely free to refuse to dispose of his stock.

But the validity of that contract was clearly a matter purely of state law; and in addition, the order adjudicating its validity (made December 4, 1936) is not here under review, and is long since final. The State courts' deter-

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[18]Emphasis in original.

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mination of the validity of the contract rests in part [*e. g.*, Juris. St. (Co.) Appx. p. 12a; Juris. St. (Gentles) Appx. p. A-13] on the adequate non-federal ground that its validity was *res judicata.*

> *City & County of San Francisco v. Itsell* (1890), 133 U. S. 65, 67.

The complaint of Appellants is that they *will be* deprived of a property interest *if* the Liquidator carries out his contract.

But again, they were afforded ample opportunity to be heard in 1936 on the question as to whether he should make that contract. As the District Court of Appeal says,

> "Petitioners (Appellants) were parties to the proceeding in which the rehabilitation agreement was proposed, and their representatives participated in seeking that approval. They may not now complain of its terms." [Juris. St. (Co.) Appx. p. 92a; Juris. St. (Gentles) Appx. p. B-35.]

III.

There Is No Constitutional Requirement That the State Afford a Contracting Party Escape From a Contract of Which He Repents.

Throughout their arguments Appellants seem to assume that the Insurance Commissioner was required to determine that the mutualization price was fully compensatory before he could properly "approve" the plan.

But the State law, as laid down by its courts, and the policy of California, is to the contrary.

The opinion of the District Court of Appeal is specific:

> "The basic problem for the Commissioner to determine was whether or not the price and terms of

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payment for the New Company stock were fixed in accordance with the mutualization agreement, for if they were, the Plan of Mutualization is fair and equitable because it gives the stockholder the price and terms he agreed to take." [Juris. St. (Co.) Appx. p. 91a; Juris. St. (Gentles) Appx. pp. B-33-4.] [See also Superior Ct. opinion, Juris. St. (Co.) Appx. p. 121a; Juris. St. (Gentles) Appx. p. C-31.]

Indeed, it is the policy of California to permit security holders who may desire to sell their securities to make their own decisions in the absence of fraud, even though a state officer might feel that they were selling at too low a price.

> *Transportation Bldg. Co. v. Dougherty* (1946), 74 Cal. App. 2d 604, 614.

California has conclusively determined that the duty of the Commissioner under her statute did not require him in the circumstances of the case, to determine that the agreed price was fully compensatory.[19]

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[19]We suggest that "approval" of a transaction by a public officer does not necessarily require an examination into the interests of all persons whose rights may be affected thereby. It depends on the purpose of the statute. Thus, where an exploration permit may not be assigned without the "approval" of the Secretary of the Interior, the assignor is not entitled to the decision of that officer that the consideration for his assignment is adequate. (Analogy suggested by *Atlantic Pacific Oil Co. v. Gas Dev. Co.* (1937), 105 Mont. 1.) An employer, contracting for an increase in wages during wage stabilization is not unconstitutionally deprived of his property by a blanket approval of all pending applications at the repeal of Stabilization. (Analogy suggested by *American Fed. of Grain Millers v. General Mills, Inc.* (D. C. Minn. 1953), 117 F. S. 340.) One who has contracted to buy property at cost plus 10 per cent, but not above the ceiling price, is not unconstitutionally deprived of his property by an increase in that ceiling price which results in his paying a higher price. (Analogy suggested by *Nesseth v. Creedon* (D. C. Minn. 1948), 80 F. S. 269.)

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No authority has been called to our attention suggesting that the State is constitutionally required to relieve a contracting party of his contract merely because he later considers it to have been unwise.

IV.

There Was Ample Evidence That the Price Fixed Was Adequate.

As the State courts have pointed out, the only evidence introduced before the Commissioner was that the mutualization price was adequate.[20] The witnesses were eminently qualified, and their testimony was clear.

Appellants seek to place different interpretations on some of the data, and to challenge the conclusions of the experts, on the basis of what the District Court of Appeal terms "mere unsupported suggestions and opinions of counsel."[21]

Even if the Commissioner's judgment in accepting the conclusions of the witnesses had been faulty, it would not amount to a denial of due process.[22]

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[20]*Supreme Court:* Juris. St. (Co.) Appx. p. 14a; Juris. St. (Gentles) Appx. p. A-15.

Dist. Ct. of Appeal: Juris. St. (Co.) Appx. p. 81a-83a, 92a; Juris. St. (Gentles) Appx. pp. B-25, B-35.

Superior Court: Juris. St. (Co.) Appx. pp. 122a-123a; Juris. St. (Gentles) Appx. pp. C-31-34.

[21]Juris. St. (Co.) Appx. p. 92a; Juris. St. (Gentles) p. B-35. See also the remark of Mr. Justice Carter (dissenting) to the effect that the interpretation of such data is matter for experts in the field of insurance. Juris. St. (Co.) p. 60a; Juris. St. (Gentles) p. A-68.

[22]Compare: "Error in judgment in the compromise of liabilities is not a taking of property or an impairment of contract in derogation of the restraints of the Constitution of the United States." *Doty v. Love* (1935), 295 U. S. 64, 74.

We submit, however, that the Commissioner did not err. We note some of the grosser errors in the computations produced by Appellants:

Gentles *et al.* make the fundamental error of assuming that the amount of the surplus of a company must be *added to* the capitalized value of the earnings produced by that surplus (and the other assets) in order to determine the fair value of an enterprise. [Juris. St. (Gentles) p. 27.] This error permeates many of their figures, including their table on page 28.

Their table on page 24 assumes that it is now certain (and was certain in 1948) that the condition of the company in 1974 would be that which the committee estimated. But the committee, recognizing the speculative nature of such estimates, felt that the value should be discounted at 10 per cent per annum for risk.

They assume that no mutualization is fair which does not provide for payment to stockholders not alone of an amount equal to capital and surplus at the time of the plan, but all accretions to surplus until payment is completed (p. 32)—a process which would obviously prevent any mutualization, for on payment of all capital and surplus the economy would be insolvent.[23]

They say that when the purchase price is paid New Company must have some $28,000,000 of surplus (p. 15) —and assume that the stock will then be worth that amount—without observing that the "surplus" will be supplied in large part by the Participating Department,

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[23]Reported cases indicate that the mutualization price is usually far less than capital and surplus: *e. g., Belden v. Union Central* (1944), 143 Ohio St. 329 (mutualization price $3,125,000; capital and surplus $14,800,000).

to which the stockholders have no claim. [See Rehabilitation Agreement, Art. 6, Juris. St. (Gentles) Appx. pp. F-6-10.]

They furnish (p. 34) figures which they represent as the "actual earnings" of two departments of New Company from 1949 to 1952 (which, of course, are not in the record). The figures were contained in Appellants' Opening Brief in the State courts (Op. Br. pp. 127-8). Their propriety and accuracy were challenged.[24] Appellants then abandoned those figures, but substituted (Pet. for Hear., p. 95) figures they represented as the estimated and actual figures for all departments. These figures *increased* the estimate by $1,000,000 and *decreased* the so-called "actual" by more than $1,000,000. Moreover, Appellants' "actual" figure there used had admittedly been increased by eliminating some $2,700,000 of "losses" in the group accident department. In addition, it repeated the errors of classification and duplication that had been pointed out by the witnesses before the Commissioner in discussing the 1949 figures.

The figures are not only outside the record, but are grossly inaccurate.

Appellants complain that the provisions of the Rehabilitation Agreement relative to the writing of participating and non-participating insurance have been "outrageously watered down" [Juris. St. (Gentles) p. 26 note; See also Juris. St. (Co.) p. 28]. The facts are that those

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[24]The earnings for 1949 were available at the hearing before the Commissioner. Appellants there (using figures similar to those now used) asserted that the actual earnings of the Life department were $380,000 as against $138,000 estimated. The witness showed that appellants were not using comparable figures; and that in fact the actual was (on comparable bases) $888,000 against an estimate of $877,000. [Tr. pp. 334-7; Ex. 30.]

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provisions of the Rehabilitation Agreement have always been a mere declaration of policy [Art. 20(e); Juris. St. (Co.) Appx. p. 151a; Juris. St. (Gentles) Appx. pp. F-30-31]; that they have not been (and could not have been) altered by the Mutualization Plan; and that the Mutualization Plan provides an *additional* method of enforcement. [Juris. St. (Co.) Appx. pp. 159a-160a; Juris. St. (Gentles) Appx. pp. G-12-13.]

Appellants complain that it is impossible to predict future income. [Juris. St. (Gentles) p. 33.] Such an argument would, of course, destroy all attempts to determine value by the common method of capitalizing earnings.[25] But the entire life insurance industry is predicated on the fact that it is possible to predict, with reasonable accuracy from the long range point of view, not only mortality rates, but interest rates and (generally) earnings, over a period of a lifetime—frequently 50 to 75 years, and (in the case of optional settlements) for periods which may well exceed 100 years.

Moreover, appellants are hardly in a position to object to such predictions; for, as the witnesses pointed out, other methods of valuation would have produced no more than a nominal value for the stock.

It should also be observed that it is only by assuming that the committee's estimates are certain to be realized (which the committee denied in discounting them at a 10 per cent rate for risk) that Appellants are able to produce their rather fantastic figures as to values in 1974 and later.

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[25]As Mr. Justice Holmes remarked, "The commercial value of property consists in the expectation of income from it." *Galveston v. Texas* (1908), 210 U. S. 217, 226.

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Nor are the conditions to payment unusual or unreasonable. There are only three [Juris. St. (Co.) Appx. pp. 155a-156a; Juris. St. (Gentles) Appx. p. G-8]:

1. Restoration of non-can benefits; necessarily imposed because the stockholders may not be preferred to creditors.[26]

2. That purchase fund plus capital and surplus shall exceed purchase price: necessary under California corporate law, for if payment of purchase price would exhaust capital and surplus, the Company would be insolvent.

3. That the corporation will retain an excess of assets over liabilities sufficient to enable it to continue to operate; which seems not only a reasonable but an essential condition.[27]

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[26]And, as the trial court observed, under the Rehabilitation Agreement any payment before restoration would not benefit stockholders, but would be repaid into the fund for non-can restoration. [Juris. St. (Co.) Appx. p. 120a; Juris. St. (Gentles) Appx. pp. C-29-30.]

[27]Appellants [*e. g.*, Juris. St. (Gentles) pp. 29, 32] submit arguments based on the hypothesis that it might take twenty years to accumulate such a surplus after non-can restoration is complete. Since the required surplus is rather less than that of the average company of the size of New Company [see Ex. 28, Appx. 10], it seems unlikely that the company would be able to make restoration without a surplus approximating that amount. And when it is considered that a fund is being set aside from the earnings of the Participating Department [Juris. St. (Co.) Appx. pp. 154a-155a; Juris. St. (Gentles) Appx. pp. G-6-7] to meet the purchase price; and that the Participating Department surplus is also available to meet the requirement; it appears that such assumptions are scarcely conceivable. (Note that the 5 per cent of the profits of the participating business available for purchase price are the profits of participating business written *since 1936*. The fund referred to in Juris. St. (Gentles) p. 7 (note) as unlikely to produce substantial profits is one derived only from policies written by Old Company (*i. e., before 1936*).

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Conclusion to Part IV.

We do not pause to analyze all of Appellants' attempted re-interpretation of the evidence.

The fact remains that New Company, in 1948, was earning less than $1,000,000 a year; and the non-can policies had a prior claim to $22,000,000 (plus interest) of those earnings.

The fact remains that under the ordinary methods of valuation, the stock was valueless or of only nominal value. [Ex. 28, p. 23.]

No amount of juggling undiscounted estimates of future profits will serve to disguise the fact that the price of $3,000,000, supported by the uncontradicted testimony of experts of unchallenged ability, is amply supported by the evidence.[28]

V.

There Was No Denial of Procedural Due Process.

Again, it is pointed out that there was no "deprivation" of property. But in addition, the requirements of due process were satisfied.

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[28]Appellants Gentles *et al.* refer [Juris. St. (Gentles) p. 41] to an offer to buy stock of Old Company. The offer was to buy $16,471,058 of 5 per cent redeemable preferred stock—with a sinking fund; and to buy new common stock for $528,943. Since the preferred stock would obviously be well secured, and would be redeemable, that item amounts in effect to a loan. Accordingly, the offer places a value of $1.00 a share on the existing common stock—a total of $508,200 in contrast to the mutualization price of $3,000,000.

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A. Due Process Does Not Require Court Review of Administrative Findings of Fact Reached After a Full Hearing.

Appellants were given ample opportunity to be heard before the Insurance Commissioner. There was a full and fair hearing continuing more than two weeks, resulting in a transcript of some 1500 pages. The courts have decided that the Commissioner's findings were sustained "by substantial evidence in the light of the whole record."

Due process does not require a re-examination of the factual questions in the nature of a trial *de novo*.

Alabama Commission v. Southern R. Co. (1951), 341 U. S. 341, 348.

B. There Was No Improper Dual Position; and in Any Event the Rule of Necessity Would Prevent Disqualification of the Commissioner.

As the State Supreme Court suggests [Juris. St. (Co.) Appx. p. 6a; Juris. St. (Gentles) Appx. p. A-7], the fact that Commissioner Carpenter (in 1936) consented to a plan of mutualization to be formulated by a committee, would not disqualify Commissioner Downey (in 1950) from determining the fairness of the plan so formulated.

Moreover, it has long been recognized that a statutory scheme is not to be defeated merely because of some supposed interest or bias of the only official authorized to administer that scheme.

Federal Trade Comm. v. Cement Inst. (1948), 333 U. S. 683, 701;

See:

Evans v. Gore (1920), 253 U. S. 245, 247-8;

Federal Const. Co. v. Curd (1918), 179 Cal. 489, 493-4.

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Conclusion.

We have chosen to ignore the personalities in which Appellants indulge.[29]

We cannot, however, permit to go unchallenged Appellant Old Company's attack on the motives [Juris. St. (Co.) p. 30] and actions [Juris. St. (Co.) p. 43] of Commissioner Carpenter.

Appellants do not,[30] and they cannot, refer to any matter in the record which would support those charges.

The contract made by the Liquidator in 1936 was reviewed by the courts at that time. Their order of approval has long been final. Thousands of policyholders have, in the intervening twenty years, bought policies in reliance on the option for mutualization therein contained. Its propriety is now beyond review.

The approval by the Insurance Commissioner here under review contains no element of coercion or compulsion. It deprives no one of anything.

Additionally, it is fully supported by the evidence adduced.

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[29]*E. G.*, Juris. St. (Co.) pp. 13, 14, 23, 29, 44, 49; Juris. St. (Gentles) pp. 10, 33, 41.

[30]There is reference [Juris. St. (Co.) p. 30, n. 15] to allegations of pleadings in the original Rehabilitation proceeding. They must know that those allegations have been found (expressly or by implication) to be untrue: *Carpenter v. Pacific Mutual,* 10 Cal. 2d 307; *Carpenter v. Pacific Mutual,* 13 Cal. 2d 306; *Neblett v. Pacific Mutual,* 22 Cal. 2d 393. They must know that Counsel in the Rehabilitation proceeding was censured by the California court for incorporating in his brief as statements of fact the very allegations of pleadings to which counsel for Appellant Old Company now refers. (*Carpenter v. Pacific Mutual,* 10 Cal. 2d 307, 313-4.)

We respectfully submit that no substantial federal question is presented, and that the decision rests upon adequate non-federal grounds.

The appeal should be dismissed, and certiorari denied.

Respectfully submitted,

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Attorneys for Insurance Commissioner.

FEB 29 1956

IN THE

Supreme Court of the United States

October Term, 1955

No. 584

FRANK GENTLES, *et al.*,

Appellants,

—against—

F. BRITTON McCONNELL, as Insurance Commissioner of the State of California, *et al.*,

Appellees.

BRIEF IN OPPOSITION TO APPELLEES' MOTIONS TO DISMISS

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INDEX

PAGE

POINT I. The order of the Insurance Commissioner of California was a taking of Appellants' property contrary to the 14th Amendment 1

The Superior Court in 1936 did not pass upon the provision of the Rehabilitation Agreement for advance consent of the Conservator to a plan of mutualization 7

POINT II. The constitutional questions were properly raised in the State courts 19

Unconstitutionality of the statute as construed and applied 19

The Commissioner's order as a State statute.... 24

POINT III. Appellees have not overcome any of the objections that we have made to the PDC's determination of price and terms of mutualization..... 29

Arguments pertaining to value 30

Arguments pertaining to price 33

Failure of the PDC to take account of accumulations of surplus and the earnings thereon..... 42

$250,000 per year price adjustment 45

Interest 45

POINT IV. The issues presented on this appeal, including the issues of due process which, apart from the appeal, would be reviewable by certiorari, are of sufficient importance to require decision by this Court 46

Conclusion 48

CITATIONS

PAGE

CASES:

Angel v. *Bullington*, 330 U. S. 183 ..... 3, 12
Anniston Mfg. Co. v. *Davis*, 301 U. S. 337 10
Application of Prudential Insurance Company, 132 N. J. Eq. 170 ..... 27, 28
Asbury Hospital v. *Cass County*, 326 U. S. 207 ... 11
Atchison R. R. v. *Pub. Util. Comm.*, 346 U. S. 346 ..... 25, 27
Auto Acetylene Light Co. v. *Prest-O-Lite Co.*, 264 Fed. 810, *cert. den.* 258 U. S. 622 10

Belden v. *Union Central Life Insurance Co.*, 143 Ohio St. 329 ..... 27, 28
Bondholders, Inc. v. *Powell*, 342 U. S. 921 31

Carpenter v. *Pacific Mut. L. Ins. Co.*, 10 Cal. 2d 307 *aff'd sub nom. Neblett* v. *Carpenter*, 305 U. S. 297 ..... 6, 11
Carter v. *Texas*, 177 U. S. 442 22
Case v. *Los Angeles Lumber Co.*, 308 U. S. 106 .. 16
Charleston Federal Savings & Loan Assn. v. *Alderson*, 324 U. S. 182 24
Cole v. *Arkansas*, 333 U. S. 196 22
Conn. Gen. L. Ins. Co. v. *Johnson*, 303 U. S. 77 9
Corporation Comm. v. *Lowe*, 281 U. S. 431 10

Drummey v. *State Board of Funeral Directors*, 13 Cal. 2d 75 24

Electric Bond & Share Co. v. *SEC*, 303 U. S. 419 ... 10
Estate of Kent, 6 Cal. 2d 154 3
Estate of Scott, 90 Cal. App. 2d 21 3
Eubank v. *Richmond*, 226 U. S. 137 16

Frank v. *Mangum*, 237 U. S. 309 22

PAGE

Garris v. *Mitchell*, 7 Cal. App. 2d 430 14
Grubb v. *Public Utility Commission*, 281 U. S. 470.. 12

Hansberry v. *Lee*, 311 U. S. 32 ..... 3, 9
Hutchinson v. *Coughlin*, 42 Cal. App. 664 22

In re Equitable Office Bldg. Corporation, 96 L. Ed. 1386 (not officially reported) 17
In re Prudential Insurance Company, 82 N. J. Eq. 335 27
In re 325 East 72nd St., 53 F. Supp. 997 18
International Steel Co. v. *Surety Co.*, 297 U. S. 657. 2

Lake Erie & W. R. R. v. *Pub. Util. Comm.*, 249 U. S. 422 26
Lawlor v. *National Screen Service*, 349 U. S. 322 ... 10
Live Oak Assn. v. *R. R. Commission*, 269 U. S. 354. 26
Lord v. *Equitable Life Assurance Society*, 194 N. Y. 212 27

Macallen Co. v. *Massachusetts*, 279 U. S. 620 2
Manhattan Life Ins. Co. v. *Cohen*, 234 U. S. 123 .. 24
Market Street R. Co. v. *Railroad Commission of California*, 324 U. S. 548 .....26, 27
Matter of Globe and Rutgers Fire Ins. Co., 149 Misc. 18 15
Matter of National Surety Co., 239 App. Div. 490, *aff'd*, 264 N. Y. 473 18
Matter of New York Title & Mortgage Co., 171 Misc. 489 .....15, 36, 40, 41
Matter of N. Y. Title & Mortgage Co., 168 Misc. 60 18
Matter of People (Title & Mortgage Guaranty Co. of Buffalo), 264 N. Y. 69 18
Memphis Gas Co. v. *Beeler*, 315 U. S. 649 11
Morgan v. *United States*, 298 U. S. 468 26

National Fertilizer Asso. v. *Bradley*, 301 U. S. 178 10
National Surety Corp. v. *Nantz*, 262 Ky. 413 18

PAGE

National Surety Corp. v. *Williams*, 110 F. 2d 873 .. 18
Norris v. *Alabama*, 294 U. S. 587 22
Northern Pacific R. R. v. *Dept. of Pub. Works*, 268 U. S. 39 26

Ohio Valley Water Co. v. *Ben Avon Borough*, 253 U. S. 287 .....24, 47, 48
Otis & Co. v. *S. E. C.*, 323 U. S. 624 17

Raymond v. *Chicago Traction Co.*, 207 U. S. 20 ... 22
Rice v. *Sioux City Memorial Park Cemetery, Inc.*, 349 U. S. 70 47
Rippel v. *Prudential Insurance Company*, 85 N. J. L. 395 27

St. Joseph Stock Yards Co. v. *United States*, 298 U. S. 38 .....24, 48
Scott v. *McNeal*, 154 U. S. 34 ..... 2, 3
Shelley v. *Kraemer*, 334 U. S. 1 .....16, 22
Southern Railway Co. v. *Virginia*, 290 U. S. 190 .. 26
Standard Scale Co. v. *Farrell*, 249 U. S. 571 27
Sultan Ry. Co. v. *Dept. of Labor*, 277 U. S. 135 26

Thrower v. *Kistler*, 14 F. Supp. 217 18

Ward v. *Love County*, 253 U. S. 17 11
West Virginia State Board of Education v. *Barnette*, 319 U. S. 624 22
Wheeling Steel Corp. v. *Glander*, 337 U. S. 562 22
Williams v. *Kaiser*, 323 U. S. 471 11

STATUTES:

Constitution of the United States, Amendment XIV 1, 2, 6, 10, 11, 19, 21, 22, 24, 28, 34

U. S. C. Title 5, Section 1002(c)..... 26

U. S. C. Title 28, Section 1257(2) 19, 24, 25, 26, 27, 28

DARK PAG

PAGE

California Insurance Code

Section 1057 14

Section 11526 5

Section 11527 .....5, 9, 16, 20, 26

Sections 11525-27 .....19, 20, 21

MISCELLANEOUS:

Scott, Trusts, Sections 171, 172 14

AGE BLEED THRU

IN THE

Supreme Court of the United States

October Term, 1955

FRANK GENTLES, *et al.*, *Appellants*, —*against*— F. BRITTON MCCONNELL, as Insurance Commissioner of the State of California, *et al.*, *Appellees.*	No. 584

BRIEF IN OPPOSITION TO APPELLEES' MOTIONS TO DISMISS

POINT I.

The order of the Insurance Commissioner of California was a taking of Appellants' property contrary to the 14th Amendment.

Appellees' attack upon both our grounds for appeal—and upon our position on those issues which, apart from the grounds for appeal, are reviewable by this Court on *certiorari*—rests in large measure upon the proposition that the order (or, as they prefer to call it, the "action") of the Insurance Commissioner did not effect a "taking" of Appellants' property, but only authorized private persons to carry out a transfer of property upon which they had previously agreed (NC.* 13, 17-19; Comm. 21-25); and that, therefore, no substantial federal question is raised on this appeal.

*"NC." refers to the motion of the New Company; "Comm." to that of the Commissioner.

The "agreement", by which Appellants are said to be bound, is the Rehabilitation Agreement of 1936; and its binding effect is said to result from the order of the Superior Court approving it in 1936, which is said to be *res judicata.*

The provision of the Rehabilitation Agreement that is determinative, according to the Appellees, is the Conservator's agreement that he, as sole stockholder of the New Company, would consent to any mutualization plan that might be devised by the PDC. According to the argument, the moment that agreement was made there occurred whatever taking of Appellants' property has occurred; the rights of Appellants as beneficial owners of the New Company's stock then ceased and, from that time on, their sole interest in the rehabilitation of their Company consisted of the right to receive whatever purchase price the PDC might fix for the stock of the New Company, less any part thereof that might be needed to pay creditors.

If the "taking" of Appellants' property in 1936 was an unconstitutional deprivation of property without due process of law, Appellees say we cannot complain of it now, since "constitutional issues, equally with other issues, can be foreclosed by *res judicata*" (NC. 17); and therefore, the argument runs, there was no issue of "taking" in the present case, and the courts below correctly held that the order or action of the Insurance Commissioner was a mere license, not subject to independent judicial review.

Whether in this case there has been a "taking" of property, in the sense of the 14th Amendment, is a matter that this Court will determine by an independent examination of the substance and effect of the State action. *Macallen Co.* v. *Massachusetts,* 279 U. S. 620, 625-26; *International Steel Co.* v. *Surety Co.,* 297 U. S. 657; *Scott* v. *McNeal,*

154 U. S. 34, 45. The California courts cannot nullify Appellants' federal claim by labeling the Commissioner's order as a license. *Cf. Hansberry* v. *Lee,* 311 U. S. 32; and see *Angel* v. *Bullington,* 330 U. S. 183, 190-91.

Appellees make a number of references to "consent" of stockholders. They seem to imply, without quite formulating the proposition, that—in addition to the consent of the Conservator to the Mutualization Plan—in some way the stockholders of the Old Company affirmatively consented to the terms of the Rehabilitation Agreement, and therefore are bound by it as a matter of contract. The Commissioner (Comm. 23) asserts the proposition that the stockholders "were afforded ample opportunity to be heard in 1936 on the question as to whether" the Conservator should enter into the Rehabilitation Agreement; but he goes on to support that proposition by quoting a statement of the District Court of Appeal which goes much further than the Commissioner's proposition (App. B-35):

> ". . . Petitioners were parties to the proceeding in which the rehabilitation agreement was proposed, and their representatives participated in seeking that approval. They may not now complain of its terms."

No citation to the record is given to support the quoted statement, and none could be adduced.* There is no evidence

*Appellees quote the District Court of Appeal for a number of statements that are inaccurate and even contrary to fact; but, as in the above instance, the particular quotation from the Court of Appeal goes much further than the proposition for which the Appellees cite it. That method of argumentation is likely to leave an erroneous impression. We note, therefore, that the decision and opinion of the Court of Appeal were vacated by the grant of a hearing by the Supreme Court; that under California law they are a nullity; and that, therefore, quotations from the Court of Appeal's opinion do not prove anything. *Estate of Scott,* 90 Cal. App. 2d 21, 24; *Estate of Kent,* 6 Cal. 2d 154, 156.

that the Old Company stockholders gave their consents to the Rehabilitation Agreement. They were not asked to consent; for neither the Rehabilitation Agreement nor the order of the Superior Court approving it rested, or purported to rest, upon the consent of anybody.* The transfer of the Old Company's assets to the New Company, the provision for future mutualization which would turn over Appellants' equitable interest in the rehabilitated enterprise to the policyholders, and all the other provisions of the Rehabilitation Agreement, were parts of a plan devised by the Insurance Commissioner for reorganizing a temporarily insolvent company which he had seized.

The Rehabilitation Agreement was a plan of reorganization formulated by a statutory trustee and judicially enforced by embodiment in an order of the Superior Court. Insofar as it bound policyholders, creditors and stockholders, it did so because the State, through the Commissioner and the Superior Court, exercised its soverign power to seize the Old Company's assets and lay down the conditions upon which they would be turned over to the New Company.

The taking of Appellants' property in this case was accomplished by a series of steps, which in their cumulative effect have produced the result that we claim is unconstitutional: (1) The stock of the New Company was made subject to an "option to mutualize"; and the Commissioner, as Conservator, agreed to leave the determination of price to a committee, and to accept such price and terms as the committee should fix; (2) the PDC fixed a price and terms which, as we have attempted to show in our Jurisdictional

*The order of the Superior Court approving the Rehabilitation Agreement did not rest on the consent of the policyholders, creditors or stockholders, but upon notice given to them and an opportunity to them to appear and be heard at the hearings on the Rehabilitation Plan (Ex. 8, cited in Op. Br., App. II, pp. 1-7).

Statement, were manifestly confiscatory; (3) the Commissioner approved the terms as fair and equitable, in an ostensible exercise of his judgment, while the same Commissioner, acting in his capacity as Conservator, consented to the plan—purporting to give the stockholders' consent required by § 11526(b)—but without determining *or even considering* whether it was in the best interests of the stockholders and creditors for whom he was trustee; and (4) the California courts denied independent judicial review of the price and terms, holding that the Commissioner had no more than a licensing function under § 11527. The courts contented themselves with a finding that there was substantial evidence before the PDC and the Commissioner, and that they had not acted arbitrarily; and so they thus failed to grapple with any of the questions of confiscation that were created by the Mutualization Plan.

Whatever may be said of any one step in the proceedings, the result of the totality of State action is that Appellants' equitable interest in the New Company's stock has been taken from them

(1) against their will;

(2) without any action on the part of the Conservator, as statutory trustee for the Old Company and its creditors and stockholders, to get the best price—or even a fair price—for their only asset;

(3) without any truly disinterested or independent determination of the fairness of the Plan by the Commissioner himself; and

(4) without a constitutionally adequate judicial review of the administrative finding that the Plan was fair and protected all interests.

It seems to us that there can be no escape from the conclusion that the sum total of State action, as described, violates the due process clause of the 14th Amendment, under all the authorities, from which there is no exception that we have found or Appellees have cited. The cases by which we support that conclusion are cited in the argument which follows.

The only escape from that conclusion is the one which Appellees rely on—that we are foreclosed by *res judicata* or—what amounts to the same thing—by the failure of stockholders in the 1936 proceedings to object to those provisions of the Rehabilitation Agreement of which we now complain, or to appeal from the order approving it.

There is nothing in the record to indicate that, in the hearings before the Superior Court in 1936, any stockholder did object to the provision for advance consent of the Conservator to a plan of mutualization; and it appears from the *Neblett* case* that no stockholder appealed from the order approving the Rehabilitation Plan. Thus the matter was not litigated in 1936; and the issue of whether the Old Company stockholders are now foreclosed, by *res judicata* or estoppel, from attacking on constitutional grounds the validity of the provision for advance consent of the Conservator, depends on two questions:

(1) Did the Superior Court in 1936 necessarily decide the point *sub silentio;* in other words, did the order approving the Rehabilitation Agreement necessarily approve the provision for the Conservator's advance consent?

(2) If so, could the stockholders have appealed from that approval, on constitutional grounds, in 1936?

**Carpenter* v. *Pacific Mut. L. Ins. Co.*, 10 Cal. 2d 307, *aff'd sub nom. Neblett* v. *Carpenter*, 305 U. S. 297.

Upon the plainest principles, the answer to both questions is No, and the Old Company stockholders are not foreclosed by *res judicata* or estoppel from attacking the mutualization provisions on constitutional grounds, as they did in the courts below.

The Superior Court in 1936 did not pass upon the provision of the Rehabilitation Agreement for advance consent of the Conservator to a plan of mutualization.

The Rehabilitation Agreement was carefully drawn to make it unnecessary for the Superior Court to pass upon the Conservator's agreement to consent, sight unseen, to any mutualization plan that might come out of the hopper, or his other agreements by which he curtailed his power to deal with the stock of the New Company in the best interests of his beneficiaries.* It was expressly provided, with respect to the mutualization provisions (but not with respect to any other provisions) of the Rehabilitation Agreement, that (App. F-31):

> "(f) If the provisions of this paragraph 20, or of any one or more of the subparagraphs hereof, should be contrary to law or illegal or void, *then such paragraph, subparagraph, or subparagraphs, shall be null and void,* and shall be deemed separable from the remaining covenants and agreements in this agreement contained; and shall in no way affect the validity of any of the remaining provisions of this agreement." (Emphasis ours)

It was further provided in paragraph (25) of the Rehabilitation Agreement (App. F-34) that:

E.g., paragraph (20), subparagraphs (b) and (c) (App. F-28-30).

> "(25) . . . All undertakings and obligations herein set forth as undertakings or obligations of the Conservator are made only in his said capacities *and to such extent as he had authority to make the same,* and the Conservator makes no warranty of his authority to make the same." (Emphasis ours).

Thus the parties to the Rehabilitation Agreement—the Insurance Commissioner as Conservator and the New Company—avoided having to ask the Superior Court in 1936 to approve either the mutualization provisions or any other future commitment of the Conservator. Had anyone challenged the legality of the advance consent on the ground that it was beyond the Conservator's authority, or was a breach of his statutory trust duties toward the Old Company stockholders, the objection would have been met by the conclusive argument that, if it was well taken, the provision would be null and void and the objector could suffer no harm; that the Court had not approved it, except insofar as it should be found to be a lawful exercise of the Conservator's power; and that, if there should ever be a plan to which the consent became applicable, then would be time enough to decide the issue of its validity. The pertinent authorities are cited below.

There could be no purpose in putting paragraph (20)(f) and paragraph (25) into the Rehabilitation Agreement except to insure that the validity of the mutualization provisions would not have to be litigated in 1936—or, to put the point in another way—except to insure that the order approving the Rehabilitation Agreement would not foreclose the issues to which the exceptions and reservations applied. Those provisions removed from the field of justiciable controversy in 1936 the agreement of the Conserva-

tor to delegate the determination of price to the PDC and to consent to any plan of mutualization it might devise.*

By ignoring the effect of the reservations in the Rehabilitation Agreement, and holding that the provision for advance consent was approved by the Superior Court in 1936 and was *res judicata,* the courts below have made the Rehabilitation Agreement a trap for the unwary. The stockholders were entitled to take the reservations and exceptions as meaning what they said. *Conn. Gen. L. Ins. Co.* v. *Johnson,* 303 U. S. 77, 79-80. Now, having been lulled into security by the reservations and exceptions, they find them written out of the Agreement by the California courts—with the result that the stockholders have not had their day in court to assert constitutional rights. *Cf. Hansberry* v. *Lee, supra,* p. 3.

There was another provision of the Rehabilitation Agreement that was calculated to make the issue of advance consent a non-justiciable issue in 1936, and also has proved a trap for the unwary. The Agreement provided that any mutualization plan would have to conform to the voluntary mutualization statute; and the statute at that time and ever since has required, as a condition to mutualization, that the Commissioner has to approve the plan after first satisfying himself that "the rights and interests of the insurer, its policyholders and shareholders are protected," and "that the plan will be fair and equitable in its operation." (§ 11527, App. E-11-12).

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*Another reason why the propriety or legality of the Conservator's advance consent could not present a justiciable controversy in 1936 is that the Mutualization Plan was to be formulated "in accordance with the laws of the State of California in effect at the time" when the request for mutualization might be made, *i.e.,* between July 1, 1946, and January 1, 1948; and no one could know in 1936 what the statute might provide 10 years later.

If any stockholder in 1936 had been able to imagine a situation in which the advance consent of the Conservator would be held to reduce the Commissioner's duty under § 11527 to the ministerial level for which Appellees now argue,* and had raised the question of due process under the 14th Amendment, he would of course have been told that it must be presumed (a) that the Commissioner would act lawfully when the time came; (b) that the measure of judicial review of the Commissioner's findings would conform to constitutional requirements; and (c) that whatever the laws of California, as in force 10 years later, might require to be done would be done. *Cf. Electric Bond & Share Co.* v. *SEC*, 303 U. S. 419, 443; *Anniston Mfg. Co.* v. *Davis*, 301 U. S. 337, 354-55; *National Fertilizer Asso.* v. *Bradley*, 301 U. S. 178; *Corporation Comm.* v. *Lowe*, 281 U. S. 431, 438.

The sum and substance of the matter, as we see it, is that the Rehabilitation Agreement was framed to make it unnecessary—and in fact legally impossible**—for the issue of advance consent of the Conservator to be litigated in 1936; and it was not litigated, *and could not have been litigated;* but that the courts below, in violation of due process requirements, have held the Appellants to be bound by that provision nevertheless.

If, as we contend, the advance consent of the Conservator is part of the totality of State action which has

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*All the Commissioner had to do, according to Appellees (NC. 14), was to say: "I find nothing wrong with the plan from any official standpoint; the Company may, therefore, proceed with the remaining steps to voluntary mutualization."

**There is no more settled principle in the law of *res judicata* than that the doctrine cannot apply to situations where the events needed to make a controversy justiciable had not yet occurred at the time of the former judgment. *Lawlor* v. *National Screen Service*, 349 U. S. 322, 328; *Auto Acetylene Light Co.* v. *Prest-O-Lite Co.*, 264 Fed. 810, 815, *cert. den.* 258 U. S. 622.

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resulted in a deprivation of property without due process of law, it avails Appellees nothing to argue that *res judicata* is a matter of State law. Even if it were, this Court would examine the basis for application of *res judicata,* in order to determine whether it had resulted in a violation of federal constitutional rights; for this Court will not permit a State court, by calling something *"res judicata"*, to evade a constitutional issue upon a colorable or unsubstantial ground. See *Memphis Gas Co.* v. *Beeler,* 315 U. S. 649, 654; *Ward* v. *Love County,* 253 U. S. 17, 22; *Williams* v. *Kaiser,* 323 U. S. 471, 478.

But the issue is not an issue of State law. It presents purely a federal question, *viz.,* whether an objection to the Conservator's advance consent, as a violation of the due process clause of the 14th Amendment, could have been litigated in 1936; and that depends upon whether, upon appeal or certiorari, the issue would have been a proper one for this Court to decide. What the State courts did, or could or would have done if the question had been presented to them in 1936, is beside the point. If one of the petitioners in the *Neblett* case had been a stockholder of the Old Company, and he had asked this Court to rule that the provision of the Rehabilitation Agreement calling for the advance consent of the Conservator was a deprivation of Appellants' property without due process of law, can there be any doubt about what this Court would have held?

Upon the most familiar principles governing this Court's exercise of its power to decide constitutional questions, it would have held that the stockholder's attack upon that provision of the Rehabilitation Agreement was premature. *Asbury Hospital* v. *Cass County,* 326 U. S. 207, 213-15.* There might never be a Plan, hence never a consent; and in

*See also cases cited in second footnote on page 10.

RK PAGE BLEED THRU

view of the Conservator's reservation, there might be a plan *but no consent,* because the Conservator, if advised that the advance consent was invalid, might withdraw it. An invalid consent could not have consequences until there was a mutualization plan; and it might not have any consequences even then.

The cases which Appellees cite in support of their application of *res judicata* are irrelevant to the issue. In two of them, *res judicata* (or estoppel) was applied against a party because in a prior proceeding he had had an opportunity to carry his constitutional objection to this Court and had failed to do so*. In all the others (NC. 16-17), the question was whether a prior decision was binding although erroneous or subject to a jurisdictional defect. There is no such question here. We are not attacking the 1936 order of the Superior Court. We are only pointing out what it did not decide.

Even if the advance consent were valid, it would not preclude a constitutional attack on the totality of State action for still another reason, *viz.*, that it was a *qualified* consent. As we have pointed out, it was a consent only to a plan which the Insurance Commissioner should find adequate to protect the interests of the stockholders and others interested, and which would be fair and equitable in its operation. The courts below, however, have written the condition out of the Rehabilitation Agreement. How they have managed to do that may be seen from Appellees' motions, wherein they persistently treat the Conservator as if he were the stockholder of the New Company in his own right. For example, the Commissioner says (Comm. 22):

> "The stockholder (*i. e.*, the Liquidator, in whose right Appellants sue) is manifestly not unconstitu-

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Angel v. *Bullington, supra; Grubb* v. *Public Utility Commission,* 281 U. S. 470.

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> tionally deprived of property when his property may be taken only as he voluntarily chooses to dispose of it by contract."

and throughout the motions there are other references to "stockholder" in the singular. That exercise in semantics goes back to the very beginning of the case. It appears in the decision of the Insurance Commissioner of September 22, 1950, wherein he worded his ultimate finding thus (App. D-22):

> "IT IS HEREBY FOUND AS A FACT that the rights and interests of the New Company, its policyholders, and the holder of its shares are protected under the terms of the plan hereinabove referred to, and that the plan will be fair and equitable in its operation."

The Commissioner's use of the singular, "holder of its shares," is evidence of a point of view toward Old Company stockholders—one that had been revealed in the Rehabilitation Agreement in 1936. That is probably the only reorganization plan in history that does not contain *a single reference* to the rights or interests of stockholders. The writers of that document achieved the remarkable feat of mentioning stockholders only once—in subparagraph (20)(c) (App. F-29-30) wherein it is provided that, even if the Old Company "or its shareholders" should put up the money necessary to restore non-can liabilities, discharge all the debts and lift the receivership, they still could not get back control of their rehabilitated enterprise.

The exclusion of the interests of the equitable owners of the New Company's stock from consideration is the very essence of the deprivation of property without due process in this case. No attention has been paid to the statutory

PAGE BLEED THRU

duties of the Liquidator, as laid down in Chapter 1 of the California Insurance Code dealing with "Insolvency and Delinquency":

> "*1057. Commissioner deemed trustee.* In all proceedings under this article, the commissioner shall be deemed to be a trustee for the benefit of all creditors and other persons interested in the estate of the person against whom the proceedings are pending."

Whatever the California Supreme Court *said* in its opinion, what it *did* by its decision was to uphold the Conservator in a breach of his trust duties under the statute.* It sanctioned the Commissioner's action in consenting to the Plan, solely because his predecessor had agreed to give consent and thus had abdicated his trust *in limine*. Had the Commissioner as Conservator paid attention to his trust duties, he not only would have examined and studied the Mutualization Plan for its fairness to Old Company stockholders, but the separate counsel by whom he was represented, in his capacity as Conservator, would have appeared at the hearing on the fairness of the Plan to assert the rights and safeguard the interests of those for whom their client was trustee. Unlike the Old Company and its stockholders, the Conservator had full access to the books and records of the New Company, which was his creature; and at the hearing he could have subjected the Mutualization Plan to critical examination, in the light of all the available facts. Instead, the Conservator's counsel failed even to enter

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*The Commissioner as Conservator and as Liquidator of the Old Company, a position which he still occupies, has been and is trustee with the duty "to conserve and protect" the interests of those who are properly entitled to share in the assets of the trust estate. *Garris v. Mitchell*, 7 Cal. App. 2d 430. Cf. Scott, Trusts, §§ 171, 172 at p. 916 (1939).

DARK PAGE

an appearance at the hearing. Compare that lack of interest with the positive roles that counsel for the New York Superintendent of Insurance, as Liquidator, have played in comparable cases in that State.*

Both the California Supreme Court and the Appellees, in dealing with the Conservator's consent to the Plan, have reasoned in a circle. The consent given by the Conservator, because of his predecessor's 1936 contract and without reference to his duty as statutory trustee, is validated by the fact that the Commissioner has found the Plan to be fair. There is thus no *improper* taking of Appellants' property. At the same time, the Commissioner's limited review of the Plan is held to be sufficient because, the Conservator having consented, the Commissioner's duties were only those of one who is called upon to license a voluntary arrangement proposed by private parties, and were not the duties of one who must pass on a "taking" of property. Thus there was no "taking" of Appellants' property *at all;* and thus the approval by the Commissioner validates the consent of the Conservator, and the consent of the Conservator validates the approval by the Commissioner.

But the inescapable fact is that the property of Appellants has been "taken" without their consent, and without an opportunity for the judicial review appropriate when issues of confiscation are involved.

Here the real parties in interest neither agreed to a price nor waived their right to an equitable price and fair terms. The price and terms have not been approved by them, and have not been fixed in fair bargaining by their trustee. They have been fixed by a Committee of third parties having no duty toward the stockholders, and whose

*E.g., *Matter of New York Title & Mortgage Co.*, 171 Misc. 489; *Matter of Globe and Rutgers Fire Ins. Co.*, 149 Misc. 18.

AGE BLEED THRU

interests were, if anything, adverse to those of stockholders. They have been approved by the Conservator, not on the merits, but because his predecessor in 1936 agreed to buy his *cestuis* a pig in a poke.

It is idle for the Appellees to say that the Commissioner's approval did not effect a "taking" of property because it was only one step "in a series of approvals which *allows* the company to purchase its own stock" (NC. 13)*. For the effect of the order of the Commissioner as a State officer was to *sanction* the taking of Appellants' interest in the New Company for the benefit of its policyholders. It was the Commissioner's "approval" of the Plan that made effective his advance consent as Conservator, and authorized the Conservator to dispose of the property of which Appellants are the equitable owners. But for the affirmative action of the Commissioner, Appellants' property could be transferred to the New Company only with their consent. The Commissioner's action, therefore, effected a taking by the State itself. *Cf. Shelley v. Kraemer*, 334 U. S. 1, 14, 19; *Eubank v. Richmond*, 226 U. S. 137.

Appellees make two further arguments designed to support their contention that there has been no "taking" of the property of the Old Company's stockholders:

> (1) That, because the Old Company was insolvent in 1936, the stockholders' equity had been wiped out; that if the absolute priority rule of *Case* v. *Los Angeles Lumber Co.*, 308 U. S. 106, had been applied, the stockholders' interest would not have been permitted to participate in a reorganization; and that, therefore, such rights as the Old Company stockholders now have were *created* by the Rehabilitation Agreement (NC. 16, 18).

*Emphasis ours.

DARK PAGE

(2) That the mutualization provisions of the Rehabilitation Agreement are a contract for the benefit of the participating policyholders, who bought the "option to mutualize" by relinquishing their right or claim to $4,792,118.97 of assets which, on the books of the Old Company, had been credited to the Participating Division of its Life Department, but were not transferred to the participating department of the New Company—$3,000,000 having been used to provide the capital of the New Company ($1,000,000) and to give it a paid-in surplus of $2,000,000, and $1,792,118.97 having been turned over to the New Company's Accident & Health Department to provide a cushion for non-can liabilities assumed by it (NC. 5-6; Comm. 9).

Both these arguments have become, by constant reiteration alone, a part of the folklore of the case. Neither has a sound legal foundation, neither accords with the facts, and neither leads to a conclusion that supports Appellees' argument that there has not been a "taking". However, it does not seem advisable to lengthen this brief by discussing either point at length. A brief comment with respect to each of them may suffice:

There has never been any true insolvency in this case (J. S. No. 584, p. 6, fn.). Indeed, the prosperous financial history of the New Company after rehabilitation is a fine justification, in the insurance company field, of the judicial view, often expressed, that reorganization and rehabilitation proceedings are designed to, and frequently do, preserve investment values and avoid premature deflation and the destruction of equities because of conditions which are temporary.*

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*Otis & Co. v. S. E. C., 323 U. S. 624; *In re Equitable Office Bldg. Corp.*, 96 L. Ed. 1386 (Aug. 6, 1946, not officially reported);

AGE BLEED THRU

The participating policyholders of the Old Company did not contribute one nickel of surplus to the New Company, because they had no surplus to contribute. The surplus had been wiped out, and the restoration of surplus was due, not to any sacrifice by the participating policyholders, but solely to the contribution which the non-can policyholders made, by accepting an indefinite deferment of various proportions of their actual and potential claims. It was the non-can policyholders whose sacrifice permitted the reduction of reserves, and thereby created the corporate surplus which was distributed among the departments of the New Company. That is made clear in Commissioner Caminetti's report to Governor Warren (Ex. 38, pp. 3-4). Instead of contributing $4,792,118.97 to the other departments of the New Company, the participating policyholders contributed nothing, and got back $423,136 of surplus contributed by the non-can policyholders—and got it back free of all claims of creditors and non-can policyholders (App. F-7).

The two points—that the stockholders' rights are derived from the Rehabilitation Agreement, and that the participating policyholders have a contract right to enforce the mutualization provisions of that Agreement—do not lead to any conclusion that helps the Appellees. All they add up to is that the stockholders are bound by the Rehabilitation Agreement. The question remains: Bound to what? What was the bargain that was made in 1936, and to what does it bind the stockholders?

National Surety Corp. v. *Williams*, 110 F. 2d 873, 877; *In re 325 East 72nd St.*, 53 F. Supp. 997; *Thrower* v. *Kistler*, 14 F. Supp. 217, 219; *National Surety Corp.* v. *Nantz*, 262 Ky. 413; *Matter of People (Title & Mortgage Guaranty Co. of Buffalo)*, 264 N. Y. 69; *Matter of National Surety Co.*, 239 App. Div. 490, *aff'd*, 264 N. Y. 473; *Matter of N. Y. Title & Mortgage Co.*, 168 Misc. 60.

We say that it binds them to everything in the Rehabilitation Agreement that was lawful and proper, but does not bind them to a provision by which their statutory trustee agreed to sell out their equity without exercising his own judgment as to its value, and whereby he abdicated the price-fixing function to three private persons—nor can it bind the stockholders to a sale of their equitable interests at a price and upon terms which they claim are confiscatory, until an appropriate judicial determination is had on the issue of confiscation.

POINT II.

The constitutional questions were properly raised in the State courts.

Our grounds of appeal are: (1) that the State statute (Ins. Code, §§ 11525-27), as construed and applied by the courts below, violates the due process clause of the 14th Amendment; and (2) that the order of the Commissioner likewise violates the due process clause, and is a statute for the purpose of appeal under Jud. Code, § 1257(2).

Appellees challenge both grounds. Insofar as that challenge is based upon the proposition that there has been no "taking" of Appellants' property, and therefore no federal question, we have dealt with it under Point I.

Unconstitutionality of the statute as construed and applied

With respect to the first ground of appeal, Appellees say that it was not raised in the court below; that there was not "an explicit and timely insistence" that the statute, as construed and applied, is repugnant to the Federal Constitution. We rest our appeal under this heading, not upon the

AGE BLEED THRU

verbal formulation in the State courts of the issue in terms of the invalidity of the State statute, but rather (a) upon the formulation of the underlying issues of construction and application of the statute, which spell out its invalidity as construed and applied, and (b) upon our contention that the California Supreme Court passed upon those issues and thereby construed and applied the statute (§§ 11525-27) to produce the unconstitutional result, of which Appellants had complained throughout the whole course of the proceedings below.*

We urge that the statute has been construed and applied unconstitutionally in the following holdings of the court below: (1) that the Conservator had the right to give the consent of shareholders required by the statute, without reference to the interests of the equitable owners for whom he was statutory trustee; (2) that he could (and did) bind himself to give that consent in advance, sight unseen; (3) that, in spite of his conflicting interests, the Commissioner as Conservator could give that consent and as Commissioner could be a judge in his own cause; (4) that in discharging his duty under § 11527 the Commissioner did not have to exercise his independent judgment on price and terms, but could rely on the judgment of a committee of three private persons, so long as their decision was not "arbitrary"; and (5) that the Commissioner's approval of the Plan under § 11527 was only a license, and therefore not subject to independent judicial review.

While the arguments in the briefs below are mingled with arguments addressed to the numerous State issues, as must almost necessarily be so when the case is complicated and the issues numerous—and while some do not stand out

*See Petition for Mandate, par. XXII, and accompanying Points of Error (2) and (3), Clk. Tr. 22, 28, 29.

as clearly as might be desired—we believe that anyone reading the briefs for Appellants in the several courts would perceive that the attack on the totality of State action related at almost every point to an issue of statutory construction which, if decided adversely to Appellants, was urged by them as a violation of due process under the 14th Amendment.*

A large part of the constitutional argument in the courts below related to whether the voluntary or involuntary mutualization statute was properly applicable. It was contended by Appellants that the involuntary statute should be applied, because it provided for procedures that were essential to due process, including appraisal of the stockholders' interests and full judicial review; and that, if the voluntary statute was properly applicable, it should be construed to require the same measure of review; otherwise an unconstitutional result would be reached. Thus the burden of the whole argument—whether or not expressed *in haec verba*—was that the construction of the statutes which made §§ 11525-27 applicable, and denied judicial review appropriate to confiscation cases, was an unconstitutional construction and application, which resulted in a violation of the 14th Amendment.

In formulating the argument that the totality of State action, including the construction of the statute, added up to a violation of the 14th Amendment, Appellants at pp. 164-65 of their opening brief in the District Court of Appeal,** after pointing out that the 14th Amendment is a limitation on State action of every character—executive,

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*Op. Br. 6-8, 180, 233-243, 288; Pet. H. 10-11; Pet. Reh. 3-4, 25.

**The same brief was filed in the California Supreme Court and was the main presentation of Appellants in that court.

K PAGE BLEED THRU

legislative, judicial and administrative—* put the argument thus:

> "But the different components of state action involved cannot be considered separately for this purpose—it is the totality of state action which determines whether there has been a deprivation of property without due process of law.
>
> "Had either the order of the Court or the order of the Insurance Commissioner by itself approved a specific Plan which required the sale of the stock at a confiscatory price, a typical deprivation of property without due process of law would have occurred. No lesser deprivation by the state occurs because that result is achieved as a consequence of the combined actions of the state court and the state Insurance Commissioner, rather than by either of them acting alone."**

Similarly, the Petition for Hearing in the State Supreme Court (pp. 2-3) stated:

> ". . . the District Court of Appeal deprived Appellants of property without due process of law and denied them the equal protection of the laws, all contrary to the Fourteenth Amendment of the Constitution of the United States and thereby ousted itself of jurisdiction."

The California Supreme Court upheld the statute as not requiring independent judicial review, and as not violat-

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*Citing *Norris* v. *Alabama*, 294 U. S. 587, 589, quoting *Carter* v. *Texas*, 177 U. S. 442, 447; *Shelley* v. *Kraemer*, 334 U. S. 1, 14-15; *Raymond* v. *Chicago Traction Co.*, 207 U. S. 20, 35-36; *West Virginia State Board of Education* v. *Barnette*, 319 U. S. 624, 637; *Hutchinson* v. *Coughlin*, 42 Cal. App. 664, 669.

**Citing and quoting from *Wheeling Steel Corp.* v. *Glander*, 337 U. S. 562; *Cole* v. *Arkansas*, 333 U. S. 196; and *Frank* v. *Mangum*, 237 U. S. 309.

ing constitutional rights because there was no "taking". The Court said (App. A-14):

> ". . . The approval of the mutualization plan by the commissioner did not involve any deprivation of property rights or vested rights; it was in essence a permit or license authorizing the new company to purchase its own stock. Under these circumstances the function of the superior court was to determine whether the action taken by the commissioner was arbitrary or constituted an abuse of discretion, and in upholding the action of the commissioner, it properly refused to conduct a trial de novo."

Justice Carter, dissenting, dealt with both phases of the constitutional issue in the following passage (App. A-62):

> ". . . This [*i. e.,* that the Commissioner's order was a mere license] *would* be true *if* new company members owned their own stock (and therein lies the fallacy in calling new company a solvent corporation with all that term connotes). But the matter is not quite so simple. All the beneficial ownership, which is the *real* ownership is held by the policyholders and stockholders of old company; all the legal title is held by the voting trustees (appointed by the commissioner) for the benefit of *old company* policyholders and stockholders. . . . We held in the Drummey case that we could see no escape from the conclusion that the court must weigh the evidence and exercise its independent judgment on the facts as well as the law, if the complaining party was to be accorded his *constitutional rights* under the state and federal Constitutions. 'The state constitutional provision discussed, *supra,* prohibits the conferring of judicial power on such administrative boards.'" (Emphasis is Justice Carter's.)

RK PAGE BLEED THRU

Thus it was Justice Carter's view that the statute, as construed to involve merely a license, the granting of which was not subject to independent judicial review, was unconstitutional; and he went on to discuss the authorities under the 14th Amendment, citing and quoting from *St. Joseph Stock Yards Co.* v. *United States,* 298 U. S. 38, 52, citing *Ohio Valley Water Co.* v. *Ben Avon Borough,* 253 U. S. 287, and pointing out that what he considered to be the governing case under California law—*Drummey* v. *State Board of Funeral Directors,* 13 Cal. 2d 75—had been decided on both state and federal constitutional grounds.

We submit that the issue of whether the statute, as construed and applied, is constitutional was raised below with sufficient clarity to be decided, and that it was decided by the California Supreme Court. If that be so, then this Court will not concern itself with how artistically the issues were formulated, but will presume conclusively that the questions were properly raised. See *Charleston Federal Savings & Loan Assn.* v. *Alderson,* 324 U. S. 182, 185-86; *Manhattan Life Ins. Co.* v. *Cohen,* 234 U. S. 123, 134.

If we are not right on that, then we submit that the issues which pertain to our first ground of appeal should be considered as a basis for the grant of a writ of certiorari.

The Commissioner's order as a State statute

With respect to our second ground of appeal—that the order of the Insurance Commissioner approving the Plan of Mutualization was an unconstitutional "statute" within the meaning of Jud. Code, § 1257(2)— Appellees argue that the Commissioner's order was not a "statute", because it did not order anyone to do anything, did not have any

DARK

general or continuing force, was not intended to have application in the future, and did no more than authorize the New Company to take the remaining steps toward mutualization; and further, it is said, we did not urge in the court below that the Commissioner's order was a "statute".

The question of whether the order of the Commissioner was a statute for the purpose of 28 U. S. C. § 1257(2) is one that arises first in this Court, and the fact that "the State court was not told it was being asked to determine the constitutionality" of the order as a "statute of the state"—"that such matter was not 'drawn in question' " (Comm. 20)—is irrelevant. The validity of the Commissioner's order (or "action") was drawn in question on every ground now relied upon in this Court*; and the only issue that now arises here is whether, as we contend, that order is to be treated as a statute under this Court's decisions interpreting that word in § 1257(2) of the Judicial Code. *Atchison R. R.* v. *Pub. Util. Comm.*, 346 U. S. 346, 348. No question involving the construction of § 1257(2) was before the courts below.

Whether the Commissioner's action was legislative in character is a question for this Court to decide; and it cannot turn on the categories employed by the State courts, or how the State court treated the action in the particular case, or how we characterized the Commissioner's functions before the State courts. We characterized the Commissioner's action as judicial or quasi-judicial, within the meaning of the California statutes governing the right of review of orders of officials; but that does not make the Commissioner's determination any less legislative in character for the purposes of § 1257(2).

*J. S. No. 584, pp. 17-21.

RK PAGE BLEED THRU

This Court has repeatedly recognized that orders of officials or administrative bodies regulating rates and other activities of businesses involve the exercise of both the judicial function and power which is legislative (or "quasi-legislative") in character. *Morgan* v. *United States,* 298 U. S. 468, 479-80; *Southern Railway Co.* v. *Virginia,* 290 U. S. 190, 197. Yet this Court has consistently treated the orders of such agencies as "statutes" for the purpose of appeal. *Sultan Ry. Co.* v. *Dept. of Labor,* 277 U. S. 135; *Northern Pacific R. R.* v. *Dept. of Pub. Works,* 268 U. S. 39; and compare Section 2(c) of the Administrative Procedure Act (5 U. S. C. § 1002(c)) which explicitly defines "rule making" (as distinguished from "adjudication") to include corporate reorganization matters.

The Insurance Commissioner made his order approving the Plan of Mutualization pursuant to a power delegated to him by the California legislature, to be exercised according to the standards laid down in § 11527 of the Insurance Code. When the Commissioner was called upon to apply those legislative standards to the particular plan submitted to him in this case, he was acting as an arm of the legislature. See cases cited in footnote, p. 27.

This Court has consistently regarded orders of that type as "statutes" from which appeals may be taken under 28 U. S. C. § 1257(2) and its predecessor statutes. In *Lake Erie & W. R. R.* v. *Pub. Util. Comm.,* 249 U. S. 422, this Court held that an order requiring a single railroad to build a single side track was a "statute"; and, in other cases this Court upon the same ground has entertained appeals from orders of State administrative agencies setting rates for one particular utility or corporation under a broad legislative standard of reasonableness. *Live Oak Assn.* v. *R. R. Commission,* 269 U. S. 354; *Market Street*

DARK P

R. Co. v. *Railroad Commission of California,* 324 U. S. 548.

In *Atchison R. R.* v. *Pub. Util. Comm., supra,* it was held that an order of the California Public Utilities Commission authorizing a plan of the City of Los Angeles for enlarging two railroad underpasses, and determining the division of costs between the railroad and the city, was a "statute" within the meaning of Section 1257(2). The order of the Insurance Commissioner here was no less an exercise of delegated legislative power than that of the Commission in the *Atchison* case.

The New Company cites six cases in support of the proposition that the Commissioner's action was not a "statute of a state" within Jud. Code 1257(2). In only one of the cases (*Standard Scale Co.* v. *Farrell,* 249 U. S. 571) was an opinion written; and that case merely holds that a particular action of the State Superintendent of Weights and Measures was purely "educational, and at most, advisory" (at p. 574). The other cases were memorandum decisions and are completely inconclusive, in view of the clear authority that is to be found on the subject in reported opinions.

Appellees dismiss with a wave of the hand the State court cases that we cited to show that mutualization has invariably been held to be a legislative function.* But those cases are very much in point. The three New Jersey cases show that the Chancellor, when given power to administer proceedings for mutualization of insurance companies, to appoint appraisers to fix the price, or permit the price to be fixed by agreement of all concerned, was held to be a

Lord v. *Equitable Life Assurance Society,* 194 N. Y. 212; *Belden* v. *Union Central Life Insurance Co.,* 143 Ohio St. 329; *In re Prudential Insurance Company,* 82 N. J. Eq. 335; *Rippel* v. *Prudential Insurance Company,* 85 N. J. L. 395; *Application of Prudential Insurance Company,* 132 N. J. Eq. 170.

K PAGE BLEED THRU

"legislative agent", whose actions could be reviewed only by the prerogative writ of certiorari; and in that connection it may be worthy of note that the constitutionality of the statute was upheld, against attack under the due process clause of the 14th Amendment, upon the ground that the price arrived at, by whatever method, was "subject to inquisition and approval by the Chancellor"—in short, that there was a right to judicial review. See *Application of Prudential Insurance Co.*, 132 N. J. Eq. 170, 176.

Appellees argue (NC. 14) that the *Belden* case (cited in preceding footnote (p. 27)), which they say is the only case "remotely similar to the present one", held that the Ohio mutualization statute "does not delegate legislative power." But the *Belden* case merely applied the familiar principle that, while legislative bodies may not delegate their powers, they may legislate in terms of general principles, enact standards, and assign to an official or an administrative body the duty of applying those standards in particular cases. The powers of the Ohio Commissioner, under the mutualization statute of that State, are similar to those of the California Commissioner under the California statute; and so it is of interest that the Ohio court called those powers "quasi-legislative and quasi-judicial" (143 Ohio St. at 342-43). That is the description that precisely fits the rate cases and the other cases (*supra*, and J. S. No. 584, p. 3), where this Court has held State official action to be a "statute of a state", under Jud. Code § 1257(2).

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POINT III.

Appellees have not overcome any of the objections that we have made to the PDC's determination of price and terms of mutualization.*

Our attacks on the methods and conclusions of the PDC raise two different types of questions—those pertaining to *value* and those pertaining to *price*. They are not the same; for we could concede that $3,000,000 was a fair valuation of the New Company's capital stock at December 31, 1948, without conceding a single one of our objections to the price and terms of payment fixed by the PDC. If the $3,000,000 price had been payable within a reasonable time after the PDC's decision, as a fixed obligation and with a reasonable rate of interest, a very different case would be presented. But disregarding the contingent character of the obligation to buy the stock, the remoteness of the time of payment, the absence of current interest, the non-compensatory rate of interest and all the other

*There is an error in our Jurisdictional Statement, to which both Appellees have called attention, and we want to correct it. The second and third paragraphs of the material on pp. 14-15 under the heading "7. Provisions for payment of the purchase price" was originally written to make the point that, because under the formula that governed the surplus that the New Company must have, before it can become obligated to buy its stock, it may be a long time before that obligation will become firm, however soon the non-cans may be paid off. Our figures on page 15 were intended only to show how large a surplus the Company would have to have before the condition respecting surplus would be met. However, the third paragraph was actually phrased to present a contrast between the total required surplus and the $3,000,000 price.

That, as Appellees point out (NC. 27, footnote; Comm. 29, footnote), is not a fair comparison, because any total surplus figure for the Company will include surplus of the Participating Life Department, in which the stockholders do not have the beneficial interest. Hence we request that the last sentence be considered as withdrawn and stricken.

K PAGE BLEED THRU

objections to the Mutualization Plan, it is a basic fact that it does not even provide for a payment having a value of $3,000,000 as of December 1948.*

Arguments pertaining to value

The arguments of Appellees on the matter of value are:

(1) That the PDC were experts, that they made a careful study of the earning power of the New Company, and therefore their figures can be relied on.

(2) That no countervailing evidence of value was put in by the opponents of the Mutualization Plan.

(3) That PDC members testified that, if they had valued the stock on either of two other bases, the value would have been less and there might not have been any value. The two bases suggested were:

(a) So many times current earnings in 1948, taking as the standard the times-earnings basis on which other life insurance stocks were then selling. (This, it is said, would have yielded no value, after

*The Superior Court caught that point, and in its opinion said (App. C-33-34):

"PDC might well have approached the problems presented to it and resolved those problems differently than they did. We may not agree with their approach or with their reasoning, but we cannot say, nor could the Commissioner say, that they acted without reason, and neither the Commissioner nor this Court can substitute his or its reasoning for that of the committee.

"I have arrived at this last conclusion reluctantly because of the fact that all the shareholder presently receives under the plan is a conditional promise to pay a sum of money at a distant date in the future and this promise has a *present value*, if the sum to be paid is discounted, for interest only, at 3%, *much less* than the sum which the committee finds to be the present value of the stock." (Emphasis ours.)

DARK P

making allowance for the non-can liabilities as the PDC estimated them.)

(b) So many dollars per $1,000 of insurance in force, that being said to be a rule of thumb sometimes used in buying and selling insurance companies. (That basis, it is said, would have yielded either no value or only a small value—depending upon the number of dollars per $1,000 used as the multiplying figure—again after deducting the estimated non-can liabilities.)

We comment briefly on Appellees' points:

(1) Experts, as every appellate court knows, are sometimes the most unreliable readers of the future (see *Bondholders, Inc. v. Powell,* 342 U. S. 921, 925-26*); and the reason is not hard to find. They must estimate all future factors on the most conservative basis, and the underesti-

*The following remarks of Mr. Justice Frankfurter, dissenting from the denial of certiorari in the *Powell* case, are fully applicable, *mutatis mutandis,* to the present case:

"For what the Seaboard situation proves is not the mischance of a mere guess. It calls into question the whole process of dealing with this problem. The estimates that have been so vastly negatived by the event were the product of four years of intensive study by a Special Master, qualified as a specialist in railroad affairs, with special knowledge of the Seaboard, estimates confirmed by a vast judicial apparatus. And the Seaboard is not an isolated case. In other railroad cases post-prediction earnings over a substantial period are far above the estimates on which extinction was decreed against junior securities. Indeed, the records of these railroad reorganizations at the hands of the Interstate Commerce Commission and special masters and courts have inevitably aroused deep skepticism as to expertise in this field, or, at least, as to reliance in decreeing drastic forfeitures on the basis of it. It is not to be wondered that both the Executive and the Congress have recorded dissatisfaction with the heavy incidence of forfeiture decreed by courts, not by virtue of specific authorization but as a matter of judicial administration."

K PAGE BLEED THRU

mates of factor after factor in the problem are compounded in a geometric proportion. The expertise of the PDC might be more convincing if it had survived a critical examination by the Conservator and his counsel, acting in the interests of those for whom he was a statutory trustee.

(2) The attorney for the Stockholders' Committee did not put in evidence on valuation before the Commissioner, but confined himself to cross examination and argument. That fact, however, does not make the PDC's methods of arriving at *price* any better; and it is our contention that those methods are unsound and unconstitutional *on their face.*

As a matter of fact the Commissioner did have before him evidence of value that was far more tangible, solid and convincing than the actuarial speculations of the PDC. It was an offer by American National Insurance Company, a responsible corporation, 82% controlled by one of the wealthiest men in the country (Mr. W. L. Moody, of Texas), to pay $3,000,000 for the New Company's stock immediately, to apply all available earnings to non-can restorations for 7 years, and at the end of 7 years to pay into the Company, as a contribution to surplus, whatever balance might be necessary to restore the non-can benefits in full.* On the PDC figures, that was an offer to pay something over $18,000,000 for the Company, of which $15,000,000 would go to non-can policyholders, or to reserves for their claims, and $3,000,000 would go to creditors and stockholders.** As the Committee's figures

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*Tr. 809-10, 817-18, 847-51; App. D-9-10.

**The PDC took the value of the non-can liabilities as $22,000,000, a total that is reached approximately by adding up the figures in the sixth column on Chart I (J. S. No. 584, op. p. 12). If we deduct from the total the figures for the 7 calendar years following

were too conservative, our $18,000,000 figure is an overstatement; but as the PDC had not suggested even the remotest possibility that non-can restorations could be completed in 7 years, Mr. Moody's offer for the equity of the Company could hardly be figured at less than $10,000,000 in sum total.

The Commissioner ruled that the offer could not be entertained because of the "option to mutualize".

(3) The fact (if it were a fact) that, on two other bases of value mentioned by two members of the PDC in their testimony before the Commissioner, the PDC might have arrived at less than $3,000,000 (and maybe zero) as the December 31, 1948, value, would at best be an academic argument. The PDC did not use those other bases of value, but found them inapplicable (Tr. 143, 146-47; Ex. 28, p. 25); the propriety of using them has not been litigated; and both of them ignore the most fundamental factor in determining value—the future prospects of the business. No estimate which simply multiplies 1948 earnings by a number—and no rule of thumb that values a company at so many dollars per $1,000 of insurance outstanding—can have the slightest relevance unless the 1948 figures are weighed in the light of reasonable future expectations—the probable trend of earnings or volume of business, as the case may be.

Arguments pertaining to price

While we have attacked in several particulars the methods used by the PDC to get at values, and at the

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Mr. Moody's offer (1951-57), we get $6,926,000; and deducting that from $22,000,000 we get $15,074,000 as the non-can liabilities which, if the Committee's figures turned out to be accurate, Mr. Moody's company would have had to pay at the end of 1957.

AGE BLEED THRU

underlying figures from which it derived values, our arguments on those matters are quite subordinate to those that relate to *price.*

The first of the arguments pertaining to price relates to the application of the 10% compound discount rate to reduce the estimated 1974 value of the equity, which on the PDC's figures is $27,700,000, to a 1948 value of $3,000,000. We will restate our position on this point for the sake of clarity:

(1) It is a violation of due process under the 14th Amendment for a public authority to order or sanction a taking of property at a contingent future date, for a price equal to its value at a date many years before.

(2) Putting the matter in terms of figures, it is a violation of due process to fix, by whatever means or methods, a price of $3,000,000 plus interest—to be paid when the property is taken sometime after 1974—in the face of a finding that the expected 1974 value of the property is $27,700,000.

(3) It is a violation of due process for a public authority to fix or sanction a *present* taking of property (or, as here, a taking "as of December 31, 1948," a past date) for no consideration other than a conditional promise to pay its present (or, as in this case, a past) value at a remote and contingent future date, subject to conditions that may never occur.

(4) It is a violation of due process for a public authority to say to a citizen: Your property today is worth $25,000,000, less a contingent liability of $22,000,000 that must be discharged out of earnings, so that the net present value is the difference—$3,000,000.

DARK F

When your $22,000,000 liability has been discharged, and the value of your company is at least $25,000,000 without any deduction, we will buy it and pay you $3,000,000 plus interest.

Those propositions seem so clear from the authorities, and from the standpoint of common sense, fair dealing and public morality, that they seem almost impossible to answer; and Appellees have not been able to answer them.

The Commissioner does not make any attempt to answer them. He calls our figures for future values "rather fantastic"* (Comm. 28). But the only figure that relates to the present point is the $27,700,000 figure mentioned above; and that is not our figure. That is the 1974 value, upon a 10% compound discount basis, of the PDC's own estimates of earnings from 1974 to the end of time.

Faced with a line of constitutional authority that is unanimous to the effect that, when property is taken, it must be paid for at the date of taking or within a reasonable time thereafter, the Commissioner does not deal with the point or even mention it. Nor does he mention the closely

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*Appellees also attack certain figures that we took from the brief of Appellants below, to contrast the PDC's estimates of earnings with what we understood to be the earnings that actually were realized by the New Company in the years from 1949-1952 (see J. S. No. 584, p. 34).

Whether the figures are correct, and whether they present a true picture, are matters of controversy between opposing counsel in the court below. We need not become involved in that controversy, because the figures can be disregarded without impairing the points that we intended to make, *viz.*, (1) that the amounts available for non-can restorations have exceeded the PDC's estimates by substantial amounts; and (2) that the earnings of the New Company and its volume of business have run far above the PDC's estimates. If the case comes before the Court for argument, both those points can readily be established by reference to the New Company's annual reports, which are matters of public record.

K PAGE BLEED THRU

parallel case of *Matter of New York Title & Mortgage Co.*, 171 Misc. 489, which we cited (J. S. No. 584, p. 25).

The New Company does deal with the point, devoting a little over one page to it (NC. 22-23), with an argument truly remarkable for its lack of content. As we read the argument, it embodies the following propositions:

> (1) That the courts below construed the Rehabilitation Agreement as authorizing the PDC to write a mutualization plan under which, immediately upon its adoption, the Old Company and its stockholders were denuded of all rights except (a) to receive the 1948 value of their equity in the dim distant future, should the plan go into effect, and (b) to get their equity back if the plan should fail.
>
> (2) That it was proper for the PDC to take December 31, 1948, as the valuation date, because it ordered that interest should commence to accrue from that date.
>
> (3) That the rights of the Old Company stockholders are those of people whose trustee has sold property and taken back a purchase money mortgage to secure payment of the purchase price.*

Taking the third proposition first, one has to have a vivid imagination to conceive of a situation in which a trustee could lawfully sell property for $3,000,000, payable if, as and when—by the elimination of a $22,000,000 contingent obligation—the property has acquired a value of $25,000,000; or a situation in which a trustee, having

*There is an additional argument, in the last sentence (NC. 22-23), that we deal with separately below.

found that a property will be worth $25,000,000 in 25 years, sells it now for $3,000,000, to be paid with non-compensatory interest at the end of the 25 years.

The second proposition in the New Company's argument—that the 1948 date was proper because interest was made to run from that date—proves too much. Upon that proposition any date could be defended, provided interest started to run from that date.

The first proposition is put in terms of a construction of the Rehabilitation Agreement. But the Rehabilitation Agreement does not contain a word about dates of valuation; and Appellees do not here and did not below—nor did the courts below—refer to any provisions of that Agreement that had to be construed to determine the right valuation date. The only issue was and is: May one charged with determining a fair price for property taken by State authority fix the price at present-day value and provide for payment in the distant future? The question is purely a due process question, and has nothing to do with a construction of the Rehabilitation Agreement.

Appellees' statement that upon approval of the Plan the Conservator will turn over the stock of the New Company to voting trustees, and the interest of the stockholders in the earnings of the New Company will then cease, simply begs the question. All it does is state what Appellees have tried to accomplish by adopting a Plan that does everything that words can do to cut off the rights of the Old Company and its stockholders *ab initio*. They have proposed and approved a Plan that calls for immediate transfer of the New Company's stock to voting trustees and defines the duties of the voting trustees in such manner as to negative any possible fiduciary duty to the Old Company stock-

holders. But the fact that they have so meticulously labored to cut off the stockholders' rights does not prove, or even help to prove, that what they have tried to do is constitutional or, specifically, that the fixing of 1948 as the valuation date and indefinite deferment of payment is constitutional.

Thus it will be seen that the New Company's argument under the title "Valuation as of 1948" is no more than a series of assertions as to what they have attempted to do by means of the Plan of Mutualization, plus an assertion that the California courts *necessarily* held that what they did was authorized by the Rehabilitation Agreement. As an argument in defense of the 1948 valuation date, it proves exactly nothing. Like the Commissioner, the New Company fails to address itself to the authorities which hold that when property is taken for public use (and *a fortiori* for private purposes), it must be paid for at the time of taking or within a reasonable time thereafter (J. S. No. 584, p. 25). They do not cite—and they did not cite to the California courts—a single decided case that supports their position. Nor could they, because their position is untenable. It is a marvel that Appellees have been able to maintain it in four State tribunals.

We come now to the last sentence of the New Company's argument in support of the 1948 valuation date. It reads (NC. 22-23):

> "To estimate earnings from 1974 on and then to attempt to determine their value in 1974 by discounting them to that date, as advocated by Appellants, means that the risk between 1948 and 1974 that distant earnings will not emerge as predicted would be thrust upon the life policyholders instead of being borne by Appellants who improvidently

caused the non-can deficit which prevents earlier payment."

Before analyzing this remarkable argument, we note that we *have not* advocated estimating earnings from 1974 on, and then *attempting* to determine their value in 1974 by discounting them at 10% compound interest. We have no such proposition to sustain. All we have done is to take the PDC's figures at face value, and by application of arithmetic, to state the 1974 value of the New Company's stock in accordance with the PDC's findings. It is $27,700,000; and we draw the conclusion that a price of $3,000,000 plus interest will be grossly confiscatory in 1974, on the PDC's own figures.

Now comes the New Company and says that we cannot ask it to pay a price for its stock in 1974 which bears some reasonable relation to estimated value at the time of payment, because to do so would put on the policyholders (*i.e.*, on the New Company itself) the risk that "earnings will not emerge as predicted". That risk, as the argument runs, should be borne by the Appellants, because they "improvidently caused the non-can deficit".

There is nothing in this record to show that the non-can deficits were "improvidently caused" by the management of the Old Company—much less its stockholders—rather than by the fact that a nation of generally healthy people were overrun by a catastrophic depression, and that many of them, in California and elsewhere, found it more difficult to get employment than to have accidents or get sick, and live on their accident and health insurance. But let us assume the contrary. Let us suppose that the management of the Old Company did improvidently cause the non-can deficit. Is that a reason for marking down the 1974

PAGE BLEED THRU

value of the New Company stock from $27,700,000 to $3,000,000 plus interest?

The policyholders (*i.e.*, the New Company) did not need to be protected from the risk that earnings would not emerge as expected. Their obligations were conditional upon earnings emerging *at least* as expected; and so they took no risk. Moreover the New Company has conceded, just two pages after the above argument, that "the stock [of the New Company] was valued by the Price Determination Committee on the assumption that there was *no risk* that earnings would not emerge between 1948 and 1973 sufficient to restore non-can benefits" (NC. 24-25; emphasis ours).

But let us go on and suppose that there was a risk that the stock might not be worth $27,700,000 in 1974. By what process of reasoning do Appellees reach the conclusion that the way to transfer that risk is to discount the $27,700,000 estimate on a compound interest basis back to 1948—to mark down the value of $27,700,000 to $3,000,000 plus interest? The thread of that thought, if there is one, eludes us.

Unlike the Commissioner, the New Company does take notice of the *New York Title* case; but it dismisses the case with a quip, in a footnote as follows (NC. 22):

> "The Plan did not provide for an option as was the case in *Matter of New York Title Mortgage Co.*, 171 Misc. 489, 13 N. Y. S. 2d 214, cited by Appellants (No. 584, p. 25)."

The distinction will not do. In the *New York Title* case the Superintendent asked court approval of a plan to sell certain properties to yet unknown purchasers for certain prices, upon receipt of approvals by a certain percentage of

the creditors affected. The time for getting the necessary consents was the balance of the current year (1939) and thereafter until the Superintendent called the deal off on 90 days notice to the reorganization managers. Stockholders objected on the ground, among others, that the Superintendent was proposing to give an option to unknown persons for an indefinite period of time. The court sustained the Superintendent on his power to create such an "option" with court approval, but ruled against him on the fixing of the price in advance, saying (171 Misc. at 495-96):

> ". . . Although the price for which the Superintendent proposes to make the sale to assenting creditors must be deemed to be fair and reasonable as of the present time—no one having disputed the allegation in the Superintendent's petition that the price is fair—it may well be that during the period for which the Superintendent permits the option to remain in effect the price may, by reason of change of circumstances, become inadequate. This circumstance is, however, insufficient in itself to require the denial of the application. The rights of non-assenting creditors and stockholders may be adequately protected through the addition of a provision that the agreement of purchase shall not take effect unless the price therein specified shall have been approved by the court (on notice to all creditors and stockholders) as fair and reasonable *as of the time when the agreement would otherwise become effective through the receipt of sufficient assents from creditors desiring to participate.* In this way all non-assenters will be assured that assets in the hands of the liquidator will not be disposed of for less than their fair and reasonable value at the time of such disposal." (Italics in original)

In the *New York Title* case the postponement of the "taking" of the stockholders' property was for a compara-

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tively short time—part of a year plus a further period that the Superintendent might terminate on 90 days notice. Yet the court refused to sanction a fixing of prices on the basis of values in advance of the time of sale. The case is precisely in point.

Failure of the PDC to take account of accumulations of surplus and the earnings thereon

In our Jurisdictional Statement (pp. 27-28), we pointed out that the PDC, in estimating the earnings of the New Company from 1949 to 1974 available for non-can restorations (Chart I), deducted the sum of $190,000 from each year's earnings, in order that that amount might be added to the corporate surplus, instead of going into non-can reserves; and that, in addition, the PDC had excluded from each year's earnings all earnings resulting from the investment of the $190,000 annual additions to surplus, and all amounts earned on the reinvestment of earnings produced by the gradually increasing surplus. The Committee estimated that the $190,000 per year addition to surplus, together with the compounded earnings thereon, would produce by 1974 a total increase in the New Company's surplus of $7,260,000, that being the estimated amount necessary to keep pace with the projected levels of business.

The substance of our argument is that, when the PDC came to value the capital stock of the New Company, it did not take account of the 1949-74 earnings that were thus going into surplus to increase the stockholders' equity, and did not take account of the $7,260,000 surplus of which the stockholders would be the beneficial owners at the estimated time of purchase of the stock in 1974; whereas, if proper account of either those earnings or the resulting surplus had been taken, the PDC—according to its own

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declared methods of valuation—would have had to find the 1974 value of the Company at $7,260,000 more than its figures showed, and the 1948 discounted value at $3,500,000 more than it found, or a total of $6,500,000.

Appellees have replied to our argument by asserting that the $7,260,000 surplus as of 1974 was in fact taken into consideration in the PDC's estimates of earnings from 1974 to 2000 A.D., upon which the valuation of the stock was based; that interest on the increased surplus is included in the 1974-2000 figures of estimated earnings; and that, therefore, we are asking that that factor of value be counted twice—once as capitalized earnings and once as surplus.*

We cannot so read the record. The testimony that Appellees cite seems quite ambiguous (Tr. 545-47); and Appellees' assertion is inconsistent with Chart II (J. S. No. 584, op. p. 12). Just as Chart I excluded all earnings on amounts added to surplus from 1949 to 1974, and showed earnings on capital and surplus at the unvarying figure of $347,000 —which is 3% on the capital and surplus of some $11,000,000 existing at the end of 1948—so Chart II employs the same unvarying figure year by year. If the PDC was indeed taking into account the subsequent earnings on the 1974 increase of surplus, and on additions to surplus after 1974, it concealed the fact most effectively, by retaining in Chart II the same $347,000 figure, year after year, for earnings on capital and surplus.

However, in the limited time that we have to prepare this brief, we cannot make the study that would be required

*The Commissioner goes on to make the gratuitous statement that "This error permeates many of their figures, including their table on page 28" (Comm. 26). That is only one of the numerous exaggerations in the Commissioner's brief; as a matter of fact, the alleged error neither "permeates" nor affects in any way *any* figures in our Jurisdictional Statement *except* the table on page 28.

AGE BLEED THRU

for a positive assertion of what the facts were. Nor do we need to do so for present purposes because, even if we accept the Appellees' argument, the PDC still failed to make a proper evaluation of the stockholders' interest in the surplus that was to accumulate from 1949 to 1974.

The basic assumption of the PDC's method of valuing the New Company's stock—by discounting the sum total of earnings after 1974—was based upon the premise that the earnings from 1949 to 1974 would all be required for the restoration of non-cans, so that no part thereof would redound to the benefit of stockholders. However, it appears, and in effect it is admitted, that that premise was contrary to fact. Earnings not made available for non-can restorations were transferred to surplus and, according to the estimate, would increase the value of the stockholders' equity by $7,260,000 in 1974, the estimated date when the stock would be purchased and the price paid.* That gradually increasing surplus was an element of value in every year from 1949 to 1974, and—on the Committee's theory that future earnings are discounted *from the year in which they are derived,* the PDC should have discounted from year to year in the period 1949-1974 the amounts accruing to increase the stockholders' equity—just as they did for the earnings from 1974 to 2000.

It is not sufficient to take the accumulated increase of surplus in 1974, assume that its only bearing on price is derived from subsequent earnings thereon, and then practically *extinguish* the value of $7,260,000 by discounting the future 3% return thereon back to 1948 on a 10% compound basis.

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*We have referred uniformly to the year 1974 as the estimated date of non-can restorations, to avoid the unnecessary verbiage that would be required to make each reference to both 1974 and the alternative year of 1971.

$250,000 per year price adjustment

On pp. 23-24 of its Motion, the New Company attempts to meet our point that the $250,000 per year price adjustment, in the event of restoration of non-cans prior to the PDC's estimated date, was grossly confiscatory. They refer to the adjustment as a "bonus", and imply that the stockholders were lucky to get it—first because "The Committee would have been justified in valuing the stock and fixing the price without any provision for augmentation." Just why that is so is left to the imagination. As in so many other instances in Appellees' Motions, assertion takes the place of argument.

The other reason why the stockholders will be lucky to get the "bonus" (if they get it) is that the PDC might have provided, but did not provide, for a comparable *deduction* in the event that non-can restorations were *not* completed until after 1973.

We might reply to that argument with the Scotch proverb: *Nothing in the world is made better by the fact that it could be worse.* But Appellees concede (NC. 25) that it was the PDC's assumption (and, their argument implies, a correct one) "that there was no risk that earnings would not emerge between 1948 and 1973 sufficient to restore non-can benefits"; and so a provision for the suggested deduction was plainly not necessary.

With respect to the $250,000 per year adjustments, we stand on the argument in our Jurisdictional Statement (pp. 30-33), to which Appellees have not made a serious answer.

Interest

Our objections to the interest provisions of the Mutualization Plan are stated briefly in our Jurisdictional State-

ment, pp. 29-30. Under the decisions of this Court, which we cited, the points are almost self-evident.

Appellees' reply (NC. 24-25) is that interest on the purchase price of the New Company's stock was properly figured at a "no risk" rate, because there *is no risk* that earnings will not emerge between 1948 and 1973 sufficient to restore non-cans (Compare p. 22 of the same Motion, where the risk is so serious that it must be shifted to stockholders who improvidently caused the non-can deficits); that interest is properly payable at maturity, instead of currently, because the Rehabilitation Agreement prohibits current payments (Apparently no constitutional principle can survive excision by the Rehabilitation Agreement); and that the cases we cite have no application, because they deal with present right to a sum of money "which is not the situation here" (Compare p. 22 of the same Motion, where the 1948 valuation date is defended on the ground that the New Company comes under an immediate obligation to buy its stock, subject only to postponement of the time of payment until the conditions have been fulfilled!).

It will be seen that the Appellees' arguments respecting the interest provisions of the Plan are not weighty.

POINT IV.

The issues presented on this appeal, including the issues of due process which, apart from the appeal, would be reviewable by certiorari, are of sufficient importance to require decision by this Court.

Appellees urge that the questions on which we seek review are not substantial questions of federal law. To the New Company the case is "episodic", like the Indian burial

case, *Rice* v. *Sioux City Memorial Park Cemetery, Inc.*, 349 U. S. 70, where certiorari was dismissed as improvidently granted, upon the ground that the State law had been amended to prohibit cemetery companies from refusing to bury Indians, thus depriving of all significance, except to the immediate parties, the decision below upholding one cemetery company's refusal to bury a particular Indian.

It is a far cry, we submit, from the *Cemetery* case to one which presents, in the dimensions of the present case, some of the most mooted questions of current constitutional law—questions of the proper standards and procedures for valuation of property in corporate reorganizations; the proper scope of judicial review in such proceedings; and whether decisions of this Court subsequent to *Ben Avon* are to be understood as diminishing the traditional right of independent judicial review in State proceedings wherein property is taken at a price claimed to be confiscatory.

Appellees erroneously state (NC. 29; Comm. 31) that we are complaining because the California courts did not afford a "trial de novo". What we are seeking—whether it take the form of a "trial de novo" or not—is an independent judicial review of the Commissioner's determination of the fairness of the Mutualization Plan to stockholders, rather than merely a finding that the PDC and the Commissioner had before them "substantial evidence" bearing on values, and did not act arbitrarily. As we point out in our Jurisdictional Statement (pp. 37-40), anything less than full and independent judicial determination of value or price is unknown in reorganization proceedings in this country, with the two exceptions of the ICC railroad reorganization cases and the SEC public utility holding company simplifications, where special considerations of public policy are present—which are not present here in the remotest degree.

AGE BLEED THRU

Appellees state (NC. 30) that we base our argument in this respect on *Ben Avon* and *St. Joseph Stockyards Co.* v. *United States,* 298 U. S. 38. We do rely on those cases, among others that we have cited. However their doctrine may have been limited by subsequent decisions in cases involving public regulation or where the public interest is primarily involved, there is nothing in the subsequent cases to suggest that the doctrine has been limited so that it no longer applies to cases not involving public regulation, where private property is taken and confiscation is claimed.

When Appellees urge that *Ben Avon* and *St. Joseph Stock Yards* "have been limited to their special facts" (NC. 30), they tender to this Court a constitutional issue of considerable importance.

Conclusion

This case involves constitutional questions of importance, which this Court should hear and determine on appeal. If for any reason the jurisdiction of the Court on appeal is not properly invoked, the Court in its discretion should grant a writ of certiorari to review those questions.

Respectfully submitted,

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Supreme Court, U.S.
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No. 585.

In the Supreme Court of the United States

October Term, 1955

THE PACIFIC MUTUAL LIFE INSURANCE COMPANY OF CALIFORNIA, a California corporation, SAMUEL K. RINDGE, and WILLIAM H. JACK,

Appellants,

vs.

F. BRITTON McCONNELL, as Insurance Commissioner of the State of California, F. BRITTON McCONNELL, Insurance Commissioner of the State of California, as Liquidator of The Pacific Mutual Life Insurance Company of California, and PACIFIC MUTUAL LIFE INSURANCE COMPANY, a California corporation,

Appellees.

On Appeal From the Supreme Court of the State of California.

BRIEF IN OPPOSITION TO MOTIONS TO DISMISS.

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PAGE BLEED THRU



SUBJECT INDEX

PAGE

Statement 1

A.

Jurisdiction 2

1.

The order of the Insurance Commissioner is a state statute within the terms of 28 U.S.C., §1257(2) 2

(a) Mutualization involves charter amendment, and charter amendment requires legislation 2

(b) In approving the Plan of Mutualization the Insurance Commissioner acted as an agent of the legislature 3

(c) The cases sustaining jurisdiction on appeals from orders of state utilities commissions are on all fours here 6

2.

The state mutualization statutes, as construed by the State Supreme Court, present questions reviewable on appeal under 28 U.S.C., §1257(2) 7

(a) The point was raised in the courts below 7

(b) Appellees do not meet our arguments 7

3.

Titles, rights, privileges and immunities under the United States Constitution were especially set up or claimed in conformity with 28 U.S.C., §1257(3) 10

B.

Contract and res judicata 11

1.

The Rehabilitation agreement was a contract in form only 11

2.

Paragraph 20 relative to mutualization did not limit the duties of the Insurance Commissioner in the 1950 proceeding 13

PAGE BLEED THRU

PAGE

(a) Appellees rely on the opinion of the Appellate Court which is a nullity 13

(b) The State Supreme Court did not hold that the duties of the Insurance Commissioner in the 1950 proceeding were limited by the provisions of paragraph 20 14

(c) The advance consent did not bind the Insurance Commissioner as an administrative officer 15

3.

The order of December 4, 1936, was not res judicata as to the duties of the Insurance Commissioner in the 1950 proceeding 16

(a) The order of December 4, 1936, merely approved the Rehabilitation agreement 16

(b) The State Supreme Court held that the order of December 4, 1936, was res judicata only as to the validity of the Rehabilitation Agreement 17

(c) The California cases since 1936 hold that the order of December 4, 1936, is res judicata only as to the validity of the Rehabilitation Agreement and not as to its construction 19

(d) In the present case the State Supreme Court did not construe the order of December 4, 1936, as extending to the 1950 proceedings 20

4.

The order of December 4, 1936, could not have been held to limit the duties of the Insurance Commissioner in the 1950 proceeding without violating due process 20

5.

The order of December 4, 1936, could not have been held res judicata even as to the validity of the provisions of paragraph 20 without denying appellants their day in court 22

PAGE

C.

Questions substantial 24

1.

Our arguments stand unanswered..... 24

2.

Appellees are being despoiled, not unjustly enriched..... 26

(a) The policyholders made no contribution in 1936..... 26

(b) P. D. C. went on a "frolic of its own" to the injury of appellants 27

D.

Questions important and recurring..... 28

Conclusion 29

TABLE OF AUTHORITIES CITED

CASES	PAGE
Angel v. Bullington, 330 U. S. 183	23
Belden v. Union Central Life Insurance Company, 143 Ohio St. 329	5
Bingham v. Savings, etc. Company, 101 N. J. Eq. 413, aff'd 102 N. J. Eq. 302	3, 5
Breslav v. Light and Power Co., 249 App. Div. 181, aff'd 273 N. Y. 593	3
Brinkerhoff-Faris Trust & Savings Co. v. Hill, 281 U. S. 673	25
Brooks v. Town of Potomac, 149 Va. 427	8
Caminetti v. Pacific Mutual, 22 Cal. 2d 344	19
Carpenter v. Pacific Mutual, 13 Cal. 2d 306	19
Case v. Los Angeles Lumber Products Co., 308 U. S. 106	22
Casper v. Kalt-Zimmers Mfg. Co., 159 Wis. 517	3, 5
Church v. Wilson, 152 App. Div. 844, aff'd 209 N. Y. 553	17
Consolidated Rock Products Co. v. Du Bois, 312 U. S. 510	27
Coombes v. Getz, 285 U. S. 434	2
Craft v. Davidson, 189 Ky. 378	8
Cumberland Coal Co. v. Board of Revision, 284 U. S. 23	25
Evans v. Superior Court, 14 Cal. 2d 563	15
Garrison v. Pacific Mutual, 83 Cal. App. 2d 1	20
Hansberry v. Lee, 311 U. S. 32	21, 23
Heaton v. Southern Ry. Co., 119 F. Supp. 658	21
Hill v. State, 174 Ark. 886	8
Hillsborough Township v. Cromwell, 326 U. S. 620	25
Hise v. McColgan, 24 Cal. 2d 147	15
Hitt v. State, 149 Miss. 718	8
Houston v. Eidson, 119 Fed. Supp. 778	25
Iowa Des Moines National Bank v. Bennett, 284 U. S. 239	25
Jetter v. Brown, 107 N. Y. S. 2d 856	21

DARK

PAGE

Kent, Estate of, 6 Cal. 2d 154 ..... 13, 14
Law v. Charter Institute of Patent Agents (1919), Ch. D. 276 9
Lawlor v. National Screen Service Corp., 349 U. S. 322 23
Lord v. Equitable Life Assurance Society, 194 N. Y. 212 ..... 3, 4, 5
McDonough v. Goodcell, 13 Cal. 2d 741 14
Montgomery v. Eidson, 123 Fed. Supp. 292 25
Mutual Benefit Life Ins. Co. v. O'Brien, 116 S. W. 750 26
Opinion of the Judges, In re, 50 S. D. 324 21
Pacific Mutual v. Carpenter, 13 Cal. 2d 306 12
Postal Telegraph Cable Co. v. Newport, 247 U. S. 464 21
Prudential Insurance Co. of America, In re, 82 N. J. Eq. 335 ..... 3, 4
Rippel v. Prudential Ins. Co., 85 N. J. L. 395 ..... 3, 5
Romeo v. Western Express Co., 45 N. Y. S. 2d 297 21
Royal Highlanders v. Wiseman, 140 Neb. 28 26
Schwegmann v. Neff, 218 Ind. 63 21
Scott, Estate of, 90 Cal. App. 2d 21 ..... 13, 14
Standard Scale Co. v. Farrell, 249 U. S. 571 6
Stark v. Coker, 20 Cal. 2d 839 23
State v. Gonzales, 43 N. M. 498 8
State, etc. v. Crane, 36 N. J. L. 394 8
State ex rel. Ellis v. Union Central Life Ins. Co., 13 Ohio Cir. Ct. N. S. 49, 22 Ohio Cir. Dec. 262 26
State ex rel. Miller v. Aldridge, 212 Ala. 660 8
Stierlen, Estate of, 199 Cal. 140 13
United States ex. rel. Accardi v. Shaughnessy, 347 U. S. 260 9

STATUTES

Code of Civil Procedure, Sec. 1094.5 21
Insurance Code, Sec. 1043 11
Insurance Code, Sec. 11525 21
Insurance Code, Sec. 11526 ..... 2, 21

RK PAGE BLEED THRU

PAGE

Insurance Code, Sec. 11526(a) 16
Insurance Code, Sec. 11526(b) 15
Insurance Code, Sec. 11526(c) 15, 20, 21
Insurance Code, Sec. 11526(d) 16
Insurance Code, Sec. 11527 ..... 15, 20, 21
Insurance Code, Sec. 11528 21
Insurance Code, Sec. 11529 21
Insurance Code, Sec. 11529.5 21
Insurance Code, Sec. 11531 21
Insurance Code, Secs. 11532.1-11532.8 21

TEXTBOOKS

13 American Jurisprudence, p. 230 5
44 Corpus Juris Secundum, p. 674 26
2 Freeman on Judgments (1925, 5th Ed.), Sec. 704, p. 1487 22
55 Harvard Law Review (1941), pp. 125, 133 27
68 Harvard Law Review (1955), pp. 1326, 1337-8, Ripeness for Judicial Review 6
Jaffe, Administrative Law (1953), p. 617 9
40 Michigan Law Review (1942), pp. 625, 632, The New Schoolmaster in Finance 27
Vance, Law of Insurance (3rd Ed., 1951), p. 279 26

In the Supreme Court of the United States

October Term, 1955

No. 585.

THE PACIFIC MUTUAL LIFE INSURANCE COMPANY OF CALIFORNIA, a California corporation, SAMUEL K. RINDGE, and WILLIAM H. JACK,

Appellants,

vs.

F. BRITTON McCONNELL, as Insurance Commissioner of the State of California, F. BRITTON McCONNELL, Insurance Commissioner of the State of California, as Liquidator of The Pacific Mutual Life Insurance Company of California, and PACIFIC MUTUAL LIFE INSURANCE COMPANY, a California corporation,

Appellees.

On Appeal From the Supreme Court of the State of California.

BRIEF IN OPPOSITION TO MOTIONS TO DISMISS.

STATEMENT.

Appellees' principal claims are: (a) this court is without jurisdiction; and (b) even if this court has jurisdiction appellants are foreclosed by contract and res judicata. Appellees make a number of other claims which add up to the contention that no substantive constitutional questions are presented because appellants are really being unjustly enriched, not being despoiled. Appellees do not distinguish the cases relied on by us as showing that substantial constitutional questions are presented; nor do appellees cite any cases to the contrary. Finally, appellees assert that, if substantive constitutional questions are presented, appellants are not entitled to have the case heard and determined on the merits; but the assertion is dogmatically made without supporting argument.[1]

[1]References to Jurisdictional Statement are to that filed in No. 585. References to Appendices are to those in said Jurisdictional Statement.

PAGE BLEED THRU

A.
JURISDICTION.

1.
The Order of the Insurance Commissioner Is a State Statute Within the Terms of 28 U.S.C., §1257(2).

(a) Mutualization Involves Charter Amendment, and Charter Amendment Requires Legislation.

Appellees shut their eyes to the fundamental principle of corporation law: "The right to do business as a corporation * * * is not a natural one."[2] Naturally, therefore, appellees ignore the truism that the right to incorporate or amend articles of incorporation depends upon legislative grant.

In earlier days legislatures granted special charters and amended them by special legislation. But whether a charter be granted or amended by special act of the legislature, or articles be filed or amended pursuant to general laws, the acts of incorporation or amendment necessarily are legislative; and it matters not whether the acts are performed by the legislature itself or are performed by its agents.

These elementary principles are controlling here, for mutualization takes place only when the articles of incorporation of an insurance company with capital stock are amended to eliminate the capital stock.

Section 11526 of the Insurance Code of California, therefore, provides that a plan of voluntary mutualization shall include "appropriate proceedings for amending the insurer's articles of incorporation to give effect to the acquisition, by said insurer * * * of the outstanding

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[2]*Coombes v. Getz* (1932), 285 U. S. 434, 447.

shares of its capital stock and the conversion of the insurer from a stock corporation into a nonstock corporation * * *".

The Plan of Mutualization itself contains provisions for the amendment of New Company's articles of incorporation. [Ex. 15, §IV.]

(b) In Approving the Plan of Mutualization the Insurance Commissioner Acted as an Agent of the Legislature.

Indubitably, when the California legislature provided a procedure for voluntary mutualization, which included the approval of the Plan of Mutualization, by the Insurance Commissioner, it conferred legislative power on the Insurance Commissioner.

In the leading case of *Lord v. Equitable Life Assurance Society* (1909), 194 N. Y. 212, it is held that when the legislature authorizes a "course of procedure whereby a charter may be amended" an amendment made in accordance with the procedure "is the act of the Legislature." The *Lord* case is followed in *Breslav v. Light and Power Co.* (1936), 249 App. Div. 181, 184 (aff'd 273 N. Y. 593); *Casper v. Kalt-Zimmers Mfg. Co.* (1915), 159 Wis. 517; and *Bingham v. Savings, etc. Company* (1927), 101 N. J. Eq. 413 (aff'd 102 N. J. Eq. 302).

To the same effect are *Rippel v. Prudential Ins. Co.* (1914), 85 N. J. L. 395, and *In re Prudential Insurance Co. of America* (1913), 82 N. J. Eq. 335.

All of the above cases except the Wisconsin case and one of the New Jersey cases are cited in our Jurisdictional Statement (p. 42). Appellees say the cases are not in

PAGE BLEED THRU

point, but cite no case to the contrary (N. C. p. 14).[3] The cases are, however, in point. Indeed the *Lord* case is precisely in point, and the other cases are closely in point.

In the *Lord* case, the directors, with the authorization of the holders of the majority of the stock had, by virtue of the statute, amended the charter by conferring upon the policyholders the right to vote for a majority of the directors. In holding that the charter amendment was not within the reserved power of the legislature, the court was called upon to and did pass on the question whether the action of the directors was legislative.

On that point the court said:

> *"We mention, only to overrule, the position that the legislature did not amend the charter by authorizing the directors to amend it.* When the legislature authorizes a course of procedure whereby a charter may be acquired or amended, action in conformity thereto does not create the charter or make the amendment, but both come into existence through the operation of the statute. *The amendment is the act of the legislature the same as the charter itself, and neither has existence except as conferred by statute."* (p. 238). (Emphasis added throughout.)

Nothing could be more explicit than the language of the New Jersey courts in dealing with mutualization under a statute similar to the California statute for voluntary mutualization, except that under the New Jersey statute the valuation is made by the Chancellor and not the Insurance Commissioner.

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[3]New Company's motion to dismiss is cited as "N. C.," and the Insurance Commissioner's motion as "I. C."

In *In re Prudential Insurance Company of America, supra,* it is said:

> *"The enactment * * * constitutes the Chancellor of this state as a legislative agent through whose instrumentality such proceeding shall be administered."* (82 N. J. Eq. at 336.)

In *Rippel v. Prudential Ins. Co., supra,* it is said that the *appraisement of stock in a* mutualization proceeding *"was a matter of legislative discretion, to be performed by a legislative agent."* (85 N. J. L. at 398.)

The other cases cited above, and American Jurisprudence, are scarcely less explicit.[4]

Appellees say that *Belden v. Union Central Life Insurance Company* (1944), 143 Ohio St. 329, is contrary to the cases relied on by us (N. C. p. 14). But that is not so. The *Belden* case only construes the provisions of the Ohio state constitution prohibiting the delegation of legislative power as being confined to matters of legislative policy (*i.e.,* as requiring standards to be stated in the statute), but as not precluding a statute authorizing

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[4]The passage quoted in the text from the *Lord* case, except the first sentence, was quoted with approval in *Casper v. Kalt-Zimmers Mfg. Co. supra,* where the Wisconsin Court also said: "An amendment to a charter is a legislative act—just as much so when made in pursuance of a provision in its charter or in a general law as by special act." The *Lord* case was also cited with approval in *Bingham v. Savings, etc. Company, supra,* where the New Jersey Court of Equity said: "Where the legislature authorizes a course of procedure whereby a charter may be amended, action in conformity thereto does not make the amendment, but it comes into existence through the operation of the statute. The amendment is the act of legislature, the same as the charter and neither has existence except as conferred by the statute." In *American Jurisprudence,* vol. 13, p. 230, it is said: "The legislature may authorize corporators or members of a corporation to amend a corporate charter in compliance with constitutional and statutory requirements, but though the amendment is effected by the vote of the directors or stockholders, it is really the act of the legislature * * *."

PAGE BLEED THRU

the Insurance Commissioner to pass upon the fairness and equity of a voluntary plan of mutualization.

(c) The Cases Sustaining Jurisdiction on Appeals From Orders of State Utilities Commissions Are on All Fours Here.

Just as in earlier times corporate charters were granted and amended by special legislation, so railroad rates were fixed and extensions and improvements authorized by the legislatures themselves. Later the fixing of rates and the authorization of extensions and improvements were delegated to state utilities commissions. In our Jurisdictional Statement (p. 3) we rely on decisions of this Court holding that orders of state utilities commissions fixing rates or authorizing extensions involved the exercise of delegated legislative power, and, therefore, are state statutes within 28 U. S. C., §1257(2). Appellees cite *Standard Scale Co. v. Farrell* (1919), 249 U. S. 571, to the contrary. (N. C. pp. 18, 19.) In that case, as the Court pointed out, the functions of the state superintendent under review were "educational, and at most, advisory."[5] Appellees also cite five other cases (N. C. p. 14). Although appellees do not say so, in all of those cases the appeals were dismissed without opinion. An examination of the records shows that the cases are as wide of the mark as the *Farrell* case. Moreover, it requires no little assurance to suggest that such orders, without opinion, overrule the carefully considered cases cited in our Jurisdictional Statement. We submit that the cases cited by us are on all fours here.

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[5]If appellees' interpretation of the case were correct, the decision would be out of line with many decisions of this Court, both earlier and later in time. See Davis (author of a treatise on Administrative Law); *Ripeness for Judicial Review,* 68 Harvard Law Review 1326 at 1337-8 (1955).

2.

The State Mutualization Statutes, as Construed by the State Supreme Court, Present Questions Reviewable on Appeal Under 28 U. S. C., §1257(2).

(a) The Point Was Raised in the Courts Below.

Appellees assert that the point was not raised in the California courts.

Appellees refer to the allegation in paragraph XXII of the Petition for Mandate: "Said Findings and Order of said Commissioner deprive petitioners, and each of them of property without due process of law, contrary to the provisions of the Constitution of the State of California and the Fourteenth Amendment to the Constitution of the United States." (N. C. p. 11). Appellees say these allegations were insufficient to raise the point. But appellees omit to refer to the sentence following the quoted allegation: "In this respect petitioners here refer to their Points of Error hereto attached and presented with this petition." It is hard to understand the failure to refer to this sentence. Not only is the sentence quoted in our Jurisdictional Statement (p. 40) but the only reference in the entire Petition for Mandate to the Points of Error is in that sentence. Besides, the summary of the Points of Error in our Jurisdictional Statement shows that not only the point made by us in this court as to the construction and application of the mutualization statutes, but also the supporting arguments here made, were made in the courts below (Juris. State. pp. 40-41).

(b) Appellees Do Not Meet Our Arguments.

Appellees virtually limit themselves to arguing that the Insurance Commissioner, although held by the state supreme court to have "acted as a judge in his own case",

AGE BLEED THRU

was justified on the ground of necessity. Our argument to the contrary was only cumulative. But appellees do not attempt to meet it directly. Instead they cite cases in all of which there was a public interest in upholding the particular proceeding, and either no other tribunal could be authorized to act, or prompt action was necessary (see N. C. p. 31; I. C. p. 31). But none of those conditions obtained here. Mutualization was for the benefit of the management, or at most the policyholders, and not for the benefit of the public (Juris. State. pp. 29-32, 51-52). Approval of the Plan by the Insurance Commissioner in the summer of 1950 was not a matter of public necessity. The proceeding could well have been continued, and meanwhile an impartial tribunal, such as the superior court, could have been provided by the legislature and thus made the practice in California correspond to that in New Jersey in cases of voluntary mutualization or in California, itself, in cases of involuntary mutualization.[6]

Whether or not it was necessary for the Insurance Commissioner to act as a judge in his own case, it cer-

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[6]In *State ex rel. Miller v. Aldridge* (1925), 212 Ala. 660 where all the members of a state administrative board had a conflicting interest, the court found that the matter was one with which "the public is not primarily concerned," and refused to permit the board to act on the ground of necessity, but relegated the parties to the legislature for a change in the law. The same thing was done in *State, etc. v. Crane* (1873), 36 N. J. L. 394. See also *Craft v. Davidson* (1920), 189 Ky. 378. Furthermore legislation for full judicial review, or the granting of full judicial review by the California courts under existing legislation, would have removed the constitutional infirmities in the proceeding so far as they related to the Insurance Commissioner being a judge in his own case. (*Hill v. State* (1927), 174 Ark. 886; *Hitt v. State* (1928), 149 Miss. 718; *Brooks v. Town of Potomac* (1928), 149 Va. 427; *State v. Gonzales* (1939), 43 N. M. 498.)

tainly was not necessary to constitute a P. D. C. with ties of interest with the management. Nor was it necessary for P. D. C. to carry on its investigations in secret, keep no records, and report a Plan of Mutualization (including a complicated trust indenture, which deprives appellants of the incidents of their ownership for thirty-five years) without supporting data.[7] Nor was it necessary for the Insurance Commissioner to approve the plan without exercising his own discretion.[8] Nor was it necessary for the California courts to put their *imprimatur* on the plan without weighing the evidence.[9] In short,

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[7]In *Law v. Charter Institute of Patent Agents* (1919), Ch. D. 276 at page 293 it is said: "A late Lord Justice one of great learning and wide experience—Lord Justice Farwell—once stated that he could not trust the whole bench of bishops to do justice under such conditions. With a respect for the episcopate as profound as that of the Lord Justice I adopt his language, in sharing to the full his distrust of justice administered by a tribunal sitting in private, unassisted and untrammelled by the salutary rules regulating procedure and the admission of evidence obtaining in these courts, uncontrolled by the invigorating and corrective criticism provoked and stimulated by publicity and finally wrapping up its findings in a secret communication to the department which appointed it."

[8]In *United States ex rel. Accardi v. Shaughnessy* (1954), 347 U. S. 260, it is said: "It is important to emphasize that we are not here reviewing and reversing the *manner* in which discretion was exercised. If such were the case we would be discussing the evidence in the record supporting or undermining the alien's claim to discretionary relief. Rather, ***we object to the Board's alleged failure to exercise its own discretion,*** contrary to existing valid regulations." (p. 268). (Juris. State. p. 44.)

[9]"It is also probably not without significance that despite many opportunities to do so, the Supreme Court has never expressly overruled *Ben Avon*. The Supreme Court has done a great deal to make the doctrine innocuous in situations where it could do the most damage. But it is as if the Court had concluded that it would be wise to retain the case in its armory of implements, against the day when some exceptional situation might demand its application." Jaffe: ***Administrative Law*** (1953), p. 617 (See also, Juris. State. p. 45.)

the state supreme court in construing the state mutualization statutes denied appellants a fair and open hearing by an impartial tribunal; in other words denied them their day in court.

But, regardless of whether appellants were entitled to full judicial review, on any rule of review the California courts should have ordered that the writ issue, because the record affirmatively shows that the valuation was arrived at by guess work, and a gift of $30,000,000 of appellants' money is being made to New Company, and appellants are otherwise being deprived of due process (Juris. State. pp. 19-32).

3.

Titles, Rights, Privileges, and Immunities Under the United States Constitution Were Especially Set Up or Claimed in Conformity With 28 U.S.C., §1257(3).

Our Jurisdictional Statement shows that substantial questions of substantive and procedural due process were claimed in the California courts and are presented by this appeal. (Juris. State. pp. 46-50, 52.) We made an alternative application for certiorari. (Juris. State. p. 53). Appellees make no effort to meet our alternative application for certiorari except by advancing the arguments herein referred to and shown to be without support in law or fact.

B.
CONTRACT AND RES JUDICATA.

1.
The Rehabilitation Agreement Was a Contract in Form Only.

Appellees assert that appellants not only are foreclosed by contract but are attempting to claim constitutional rights as a result of their own wrong in breaching their contract (I. C. p. 23).

These assertions are without foundation.

In our Jurisdictional Statement we show that the Conservator could not contract with his own agency, and he could not and did not undertake to execute the rehabilitation agreement until after and pursuant to the order of December 4, 1936. (Juris. State. pp. 34-36.)

The rehabilitation agreement was merely a plan of rehabilitation in the form of a contract. By its order on August 11, 1936, the court directed the Conservator to present *a plan of rehabilitation.* (Juris. State. p. 7.) The rehabilitation agreement was submitted to the court pursuant to the order of August 11, 1936. Section 1043 of the Insurance Code authorizes the Conservator, who has seized a delinquent insurance company, to rehabilitate it by entering into a rehabilitation agreement. On the face of it, the statutory provision would appear to refer only to rehabilitation agreements with third persons. But on appeal from the order of December 4, 1936, it was held that the language of the statute authorized rehabilitation agreements between the Conservator and corporations

organized by him to rehabilitate the business of a seized company. The rehabilitation agreement here, nevertheless, was no more than a plan of rehabilitation. As the California Supreme Court said, referring to its approval of the order of December 4, 1936: "The legality of the seizure and the lawfulness and propriety of *the plan of rehabilitation* have already been upheld by this court." (*Pacific Mutual v. Carpenter* (1939), 13 Cal. 2d 306, 309.) Indeed, the Insurance Commissioner, in his brief in the appellate court, refers to the rehabilitation agreement as being *a plan of rehabilitation "which takes the form of an agreement"* and *"takes its validity from the order of court of December 4, 1936."* (emphasis added). (Fold. 3, pp. 8, 9.)[10]

The idea of a hydraheaded Conservator getting a meeting of minds by having one of his tongues speak for the stockholders and the other two tongues for the creditors and policyholders respectively was apparently a little incongruous even for appellees until they found themselves in this, the court of last resort.

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[10]The remoteness from a true contract is further illustrated by the provisions of the rehabilitation agreement that upon its approval by the court all policyholders who did not affirmatively reject reinsurance within 75 days should nevertheless be legally bound (par. 24).

2.

Paragraph 20 Relative to Mutualization[11] Did Not Limit the Duties of the Insurance Commissioner in the 1950 Proceeding.

It is not clear whether appellees claim (1) that the provisions of paragraph 20 of the rehabilitation agreement relative to mutualization dispensed with anything but a *pro forma* hearing before the Insurance Commissioner, or (2) that the provisions of paragraph 20 restricted the Insurance Commissioner to determining only whether P. D. C. had been constituted in accordance with the provisions of the paragraph, and had reported the plan of mutualization in good faith (N. C. p. 18; I. C. pp. 12, 17). It makes no difference, however which position appellees stand on.

(a) Appellees Rely on the Opinion of the Appellate Court Which Is a Nullity.

Appellees rely on the opinion of the District Court of Appeal (N. C. pp. 18, 13; I. C. pp. 12, 17, 23-4). But as counsel must well know, under California law the granting of a hearing by the state supreme court after decision by the appellate court vacates the decision of the latter court and renders its opinion a nullity. (*Estate of Scott* (1949), 90 Cal. App. 2d 21, 24; *Estate of Kent* (1936), 6 Cal. 2d 154, 156; *Estate of Stierlen* (1926), 199 Cal. 140, 144; *McDonough v.*

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[11]The relevant provisions of Paragraph 20 are set forth in our Jurisdictional statement (p. 33).

Goodcell (1939), 13 Cal. 2d 741, 745.)[12] This is true because hearings are granted largely to avoid confusion in the law of the state. Where hearings are granted, the opinions of the appellate court are, therefore, not even officially reported.

(b) The State Supreme Court Did Not Hold That the Duties of the Insurance Commissioner in the 1950 Proceeding Were Limited by the Provisions of Paragraph 20.

There is no suggestion in the opinion of the State Supreme Court that the duties of the Insurance Commissioner in the 1950 proceeding were limited by the provisions of paragraph 20 as claimed by appellees.

Furthermore, the failure of the state supreme court to adopt the portion of the opinion of the appellate court relied on by appellees constitutes a repudiation of it.[13]

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[12]In *Estate of Scott* it is said: *"In re Smith's Estate,* 85 ACA 365 [a decision of the District Court of Appeal] is a nullity, the Supreme Court having granted a hearing after the decision of the District Court of Appeal. Thus the opinion of the District Court of Appeal was void and of no force and effect." In *Estate of Kent,* it is said: "When such an order of transfer is made, the opinion and decision of the District Court of Appeal is no more effective as a judgment than if it had not been rendered".

[13]See the language used by the appellate court and additional language used by the state supreme court quoted in our Jurisdictional Statement (p. 15, note 6).

(c) The Advance Consent Did Not Bind the Insurance Commissioner as an Administrative Officer.

Paragraph 20 of the rehabilitation agreement (relevant portions of which are quoted in our Jurisdictional Statement p. 33) specifically undertakes only to give advance consent by the Conservator on behalf of the stockholders; and paragraph 25 (which is quoted in full in our Jurisdictional Statement p. 34) specifically provides that the Insurance Commissioner is bound by the provisions of the rehabilitation agreement "only in his capacity as such Conservator or as Liquidator of Old Company," and "all undertakings or obligations of the Conservator are made only in his said capacities and to such extent as he had authority to make the same * * *."

The Conservator, and the Insurance Commissioner as an administrative officer, are different juristic persons (*Evans v. Superior Court* (1939), 14 Cal. 2d 563, 573-4; *Hise v. McColgan* (1944), 24 Cal. 2d 147, 156-8).

The Insurance Commissioner admitted in the state supreme court that the advance consent was not binding on him as an administrative officer (Fold. 3, I. C. Reply to Pet. for Hear. pp. 18-19).

The advance consent of the Conservator in behalf of the stockholders under Section 11526(b) of the Insurance Code did not limit the duties of the Insurance Commissioner as an administrative officer under Section 11526(c) and Section 11527 any more than it limited the directors in determining whether or not to adopt the

plan under Section 11526(a) (and the directors were nominees of the Conservator until the voting trust statute was passed in 1937), or the right of the policyholders to accept or reject the plan under Section 11526(d) (and the Conservator was trustee for the policyholders as well as the stockholders).

See Jurisdictional Statement pp. 33-34 note 20.

3.

The Order of December 4, 1936 Was Not Res Judicata as to the Duties of the Insurance Commissioner in the 1950 Proceeding.

The gist of appellees' claim is that the order of December 4, 1936 is res judicata as to the *construction* of the provisions of paragraph 20 of the rehabilitation agreement and conclusively determines that the Insurance Commissioner acting under Sections 11526(c) and 11527 in 1950 was in duty bound only to determine whether P. D. C. acted arbitrarily (See N. C. pp. 15-18; I. C. pp. 17, 23-4).

(a) The Order of December 4, 1936 Merely Approved the Rehabilitation Agreement.

The order of December 4, 1936 [Ex. 8] in general language *approved* the rehabilitation agreement and each and every part thereof; and in the words of the state supreme court affirming the order, reserved "jurisdiction over the entire proceeding." (10 Cal. 2d at p. 322.) The word *mutualization* does not appear in the order. Nor is there any reference in the order to the provisions of paragraph

20 relating to mutualization. Moreover the state supreme court, in affirming the order, mentions *mutualization* only once and then only in making a factual summary of the terms of the rehabilitation agreement. In that connection the state supreme court says: "Ultimate mutualization, in the event the policyholders so elect is also provided for." (10 Cal. 2d at p. 322.)

(b) The State Supreme Court Held That the Order of December 4, 1936 Was Res Judicata Only as to the Validity of the Rehabilitation Agreement.

The distinction between an order being res judicata of the *validity* of an instrument and res judicata of its *construction* is an obvious one. (*Church v. Wilson* (1912), 152 App. Div. 844, 851-2, aff'd 209 N. Y. 553.)

The state supreme court dealt with *validity* only and expressed itself in the following unambiguous language:

> "* * * the VALIDITY of all portions of the *rehabilitation agreement,* including the provision for advance consent *is res judicata*" (Appx. A, p. 12a).

How could the state supreme court have decided any more?

At the hearing before the Insurance Commissioner counsel for New Company introduced in evidence the order of December 4, 1936, and the rehabilitation agreement *"for the purpose of establishing the res adjudicata, if you please, of the* APPROVAL *of the rehabilitation and reinsurance agreement."* (Fold. 1, Vol. I, pp. 27-8.)

The only question argued by appellees and considered by the state supreme court was whether the order of December 4, 1936 was res judicata as to the *validity* of the provisions of paragraph 20 of the rehabilitation

agreement relating to mutualization. This is affirmatively shown by the majority opinion, as well as both dissenting opinions (Appx. A, pp. 12a, 16a, 43a, 44a, 50a). Anticipating the point appellees make here, we had undertaken to show that the order of December 4, 1936 was not res judicata as to the order of the Insurance Commissioner made in 1950 (Fold. 3, Op. Br. pp. 222-6, 229-31). Appellees ridiculed our argument. They conceded the point, but declared it was entirely irrelevant (Fold. 3, I. C. Reply to Pet. for Hear. pp. 18-19). The relevant thing, according to appellees, was whether the *provisions* of paragraph 20 had been judged *valid*. Appellees' claim before the Insurance Commissioner and in the state courts was that the provisions of paragraph 20 being valid, the P. D. C. acted solely as appraisers and, therefore, as a matter of procedural law, without regard to res judicata, the Insurance Commissioner in 1950 was limited to determining whether P. D. C. had acted arbitrarily or fraudulently (Fold. 3, I. C. Br. pp. 92-5; Fold. 1, pp. 951-966). Appellees concede that the state supreme court rejected their argument (I. C. p. 11, note 9).

P. D. C., of course, did not act merely as appraisers but exercised all the functions of a district judge, together with the functions of creditors' and stockholders' committees in a reorganization proceeding (Juris. State. p. 44).

(c) The California Cases Since 1936 Hold That the Order of December 4, 1936 Is Res Judicata Only as to the Validity of the Rehabilitation Agreement and Not as to Its Construction.

The cases subsequent to the decision affirming the order of December 4, 1936, have referred to the order of December 4, 1936 and its affirmance as merely adjudicating the VALIDITY of the rehabilitation agreement. In *Carpenter v. Pacific Mutual* (1939), 13 Cal. 2d 306, 313, the court referred to "the decision of this court upholding the *validity* of the rehabilitation order." In *Caminetti v. Pacific Mutual* (1943), 22 Cal. 2d 344, 351, 352, the court said, referring to the order of December 4, 1936: "The *lawfulness* of the plan of rehabilitation was upheld on appeal;" and in the same case (p. 359) the court said: "The order of December 4, 1936 *does no more than approve* the rehabilitation agreement and the prior actions of the Commissioner and provide for its enforcement." (emphasis added).

The California courts have also recognized that in making the order of December 4, 1936, the superior court did not, and in affirming the order, the state supreme court did not undertake to *construe* the provisions of paragraph 20 of the rehabilitation agreement. Thus in *Caminetti v. Pacific Mutual, supra,* the Supreme Court undertook to construe part of paragraph 20. This it did to ascertain whether such paragraph permitted the Liquidator to transfer the stock of New Company to voting trustees. (See 22 Cal. 2d at pp. 357-9). In an earlier case (*Caminetti v. Pacific Mutual* (1943), 22 Cal. 2d 77),

PAGE BLEED THRU

which involved the rights of policyholders who had not expressly accepted reinsurance, the court said: "The main controversy involves the *construction and application of the rehabilitation and reinsurance agreement,* dated July 22, 1936, the *approval of which* by the superior court *was affirmed* by this court in *Carpenter v. Pacific Mut. Life Ins. Co.,* 10 Cal. 2d 307." (pp. 79-80). In *Garrison v. Pacific Mutual* (1943), 83 Cal. App. 2d 1, the District Court of Appeal construed the rehabilitation agreement to determine whether New Company was liable to pay interest to creditor claimants who had declined to take reinsurance. The court said: *"The correct interpretation of Article 17 [of the rehabilitation agreement] is the solution of the present controversy."*

(d) In the Present Case the State Supreme Court Did Not Construe the Order of December 4, 1936 as Extending to the 1950 Proceedings.

The point is discussed under B 2 (b), *ante,* pages 14-15.

4.

The Order of December 4, 1936 Could Not Have Been Held to Limit the Duties of the Insurance Commissioner in the 1950 Proceeding Without Violating Due Process.

There was no justiciable controversy in 1936 as to the duties of the Insurance Commissioner under Sections 11526(c) and 11527 in 1950. In 1936 it was not known and could not have been ascertained what duties, if any, the statutes in force after 1946 would impose on the Insurance Commissioner; by 1950 Section 11526(c) might well have provided for a hearing by the superior court in cases in which all the stock of the company being mutualized was held by the liquidator of a delinquent

company,[14] as is provided for in involuntary mutualization proceedings in California, and voluntary proceedings in New Jersey. Consequently in 1936 it was not within the judicial power to construe the rehabilitation agreement as passing upon the duties of the Insurance Commissioner under Sections 11526(c) and 11527 as they might or might not be after 1946.

In *In re Opinion of the Judges* (1926), 50 S. D. 324, the court, which was authorized to render advisory opinions, refused to render such an opinion on a question assuming future changes in the law, saying:

> "Manifestly we cannot at this time render any opinion as to the general constitutionality or validity of future legislative action, the exact terms of which necessarily rest in speculation and conjecture." (p. 326).

There having been no justiciable controversy, the state supreme court could not, consistently with due process, have held that the order of December 4, 1936, was res judicata as to the construction of the provisions of paragraph 20. (*Postal Telegraph Cable Co. v. Newport* (1917), 247 U. S. 464, 473-6.)[15]

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[14]As a matter of fact many of the Insurance Code sections relating to voluntary mutualization, including both sections 11,526 and 11,527, were altered between December 4, 1936 and 1950: §11525 was amended in 1937; §11526 in 1937 and 1945; §11527 in 1937; §11528 in 1937; §11529 in 1937 and 1947; §11529.5 was added in 1947; §11530 was amended in 1937 and 1947; §11531 was amended in 1937; and §§11532.1-11532.8 were added in 1941. Section 1094.5 of the Code of Civil Procedure, providing the standards under which the order of the Insurance Commissioner was judicially reviewed, was not enacted until 1945, and was amended in 1949.

[15]To the same effect are *Hansberry v. Lee* (1940), 311 U. S. 32; *Heaton v. Southern Ry. Co.* (1954), 119 F. Supp. 658; *Romeo v. Western Express Co.* (1943), 45 N. Y. S. 2d 297; *Schwegmann v. Neff* (1950), 218 Ind. 63; *Jetter v. Brown* (1951), 107 N. Y. S. 2d 856.

PAGE BLEED THRU

5.

The Order of December 4, 1936 Could Not Have Been Held Res Judicata Even as to the Validity of the Provisions of Paragraph 20 Without Denying Appellants Their Day in Court.

In our Jurisdictional Statement we urge that res judicata could not consistently with due process have been made applicable even to the validity of the provisions of paragraph 20 (Juris. State. p. 16, note 7). Appellees' argument and authorities are restricted to an attempt to show that point is not well taken.

But appellees overlook the express reservations as to validity in subdivision (f) of paragraph 20.[10] As said in *Freeman on Judgments* (1925), 5th Ed., Vol. 2, §704, p. 1487, "in such cases the express reservation itself becomes *res judicata*." Paragraph 20, relative to mutualization, is the only paragraph in the entire instrument which contains a reservation as to validity or anything else. When a

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[10]Subdivision f of paragraph 20 is as follows: "If the provisions of this paragraph 20, or of any one or more of the sub-paragraphs hereof, should be contrary to law or illegal or void, then such paragraph, subparagraph or subparagraphs, shall be null and void, and shall be deemed separable from the remaining covenants and agreements in this agreement contained; and shall in no way affect the validity of any of the remaining provisions of this agreement." In *Case v. Los Angeles Lumber Products Co.* (1939), 308 U. S. 106, the contention was made that proceedings under 77B were controlled by a prior contract. The contention was answered by the court as follows: "No conditions precedent to enjoyment of the benefits of §77B can be provided except by the Congress. To hold otherwise would be to allow reorganizers to rewrite it so as to best serve their own ends." (p. 129).

court has expressly reserved an issue for future determination, obviously it can not properly be said by some other court at a future time that the judgment in the original action is res judicata as to the issue reserved. (*Stark v. Coker* (1942), 20 Cal. 2d 839, 843.)[17]

None of the cases cited by appellees deal with reservations in the underlying documents. Nor do any of appellees' cases involve situations in which there was no justiciable controversy. Nor do any of appellees' cases conflict with *Hansberry v. Lee* (1940), 311 U. S. 32 and other cases cited by us (Juris. State. p. 32, Note 18) holding that this court will reexamine documents to ascertain for itself whether the application of res judicata involves a deprivation of due process. Indeed in *Angel v. Bullington* (1947), 330 U. S. 183, 190, a res judicata case cited by appellees, it is said "a state court cannot sterilize federal claims by putting on the adjudication a local label."

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[17]It was natural that there should be reservations in paragraph 20. In 1936 possible mutualization was more than ten years in the future, and obviously had nothing to do with the rehabilitation of the business of Old Company. That was accomplished by scaling down non-can liabilities. (Juris. State. pp. 8, 30). There were no allegations in the pleadings in the 1936 proceeding relative to the provisions for mutualization in paragraph 20. (Appx. A, pp. 46a-47a). At most, therefore, the approval of paragraph 20 by the general language of the order of December 4, 1936, was *pro forma* and insufficient to constitute res judicata as to validity even without the reservations. (*Lawlor v. National Screen Service Corp.* (1955), 349 U. S. 322, 327, Note 12).

C.
QUESTIONS SUBSTANTIAL.

1.
Our Arguments Stand Unanswered.

Appellees do not face up to our positions. Thus, appellees assert that P. D. C. was enabled to forecast earnings beginning twenty-five years in the future and thence to perpetuity (N. C. p. 21) but appellees ignore the uncontradicted affirmative evidence to the contrary (Juris. State. pp. 19-21) and disregard the authorities to the contrary (Juris. State. p. 21, note 9; pp. 46-7). Appellees assert that it was proper to select the discount rate by formula because the Insurance Commissioner was an expert (N. C. pp. 28-9), but appellees ignore the authorities holding that rates cannot be arrived at by *expertise* alone (Juris. State. pp. 21-2, 47) and disregard the fact that the Insurance Commissioner had no *expertise,* because neither he nor any other insurance commissioner in California had ever valued an insurance company in a mutualization proceeding; and he did not even attempt to exercise his own discretion. (Juris. State. p. 44.) Appellees assert that no vested interests were involved because the order of the Insurance Commissioner was permissive only (I. C. p. 21; N. C. p. 19) but they ignore the uncontradicted affirmative evidence that the compulsion resulted from the order of the Insurance Commissioner alone (Juris. State. pp. 32-7), and disregard the rule of law that even though the compulsion might have resulted from both the order of December 4, 1936, and the order of the

Insurance Commissioner taken together, this Court, on the question of due process, is concerned with the totality of the state action (Juris. State. p. 36).[18] Appellees assert that Old Company, representing the stockholders' interest, is not the equitable owner of New Company (N. C. p. 18) but ignore the California decisions since 1936, including the decision of the state supreme court in the pending case, that the Conservator was, and the Liquidator is, trustee for policyholders, creditors and stockholders alike (Appx. A, p. 2a). Appellees assert that creditors come ahead of the stockholders (I. C. p. 5) but omit to state that the creditors' claims aggregate less than $560,000 (Fold. 2, pp. 140-1). Finally, appellees are silent as to our principal arguments that substantial questions are presented (Juris. State. pp. 46-53); and do not distinguish the supporting cases cited by us (Juris. State. pp. 46-50), or cite any cases to the contrary. In short, appellees fail to meet our arguments.

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[18]Additional cases in which state action has been held violative of due process because of a condition arising from earlier state action, which has itself become final, include: *Brinkerhoff-Faris Trust & Savings Co. v. Hill* (1930), 281 U. S. 673 (decision of state supreme court, otherwise unobjectionable, held to violate procedural due process because of its effect in the light of earlier decisions of the same court); *Cumberland Coal Co. v. Board of Revision* (1931), 284 U. S. 23; *Iowa Des Moines National Bank v. Bennett* (1931), 284 U. S. 239; *Hillsborough Township v. Cromwell* (1940), 326 U. S. 620, 623 (tax assessments, otherwise unobjectionable, held to violate substantive due process where assessments on other comparable property (which had become final) had intentionally been made on a more favorable basis of valuation); *Houston v. Eidson* (1954), 119 Fed. Supp. 778; *Montgomery v. Eidson* (1954), 123 Fed. Supp. 292 (orders remanding convicts to prison, otherwise proper, held to violate due process when made after final orders of other state courts granting writs of habeas corpus).

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2.

Appellees Are Being Despoiled, Not Unjustly Enriched.

(a) The Policyholders Made No Contribution in 1936.

Appellees assert that the participating life policyholders made a contribution of almost $5,000,000 to the reorganization and suggest that the policyholders other than non-cans are therefore entitled to a windfall profit of $30,000,000 on mutualization (N. C. p. 6). This assertion obviously attempts to contradict the terms of the rehabilitation agreement and the order of December 4, 1936, approving it which gave the par and other policyholders, except non-cans, full insurance in a solvent company, but gave them no more. The assertion is also without any basis in fact. The alleged contribution was merely a bookkeeping operation, and was specifically so treated in the Rehabilitation Agreement [Ex. 9, Par. 6] and in the Order of December 4, 1936 [Ex. 8, Par. 11]. Besides, neither the articles of incorporation nor the by-laws of Old Company gave par policyholders a lien or charge on the reserves carried on par policies. Nor did the par policies themselves provide for a lien or charge on the reserves [Fold. 1, pp. 571-6]. Consequently, as a matter of law, the reserves carried on par policies were general assets of Old Company. There is no conflict in the authorities on that point.[19] Moreover, if par policyholders made the alleged contribution of almost $5,000,000 to the reorganization, why were all policyholders other than non-cans treated alike?

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[19]See Vance: Law of Insurance (3rd Ed. 1951), p. 279; *State ex rel. Ellis v. Union Central Life Ins. Co.* (1910), 13 Ohio Cir. Ct. N. S. 49, 22 Ohio Cir. Dec. 262, 265-6; *Mutual Benefit Life Ins. Co. v. O'Brien* (Ky. 1909), 116 S. W. 750; *Royal Highlanders v. Wiseman* (1941), 140 Neb. 28, 38-9; 44 *C. J. S.* 674.

(b) P. D. C. Went on a "Frolic of Its Own" to the Injury of Appellants.

Appellees assert that on any method of valuation except that used by P. D. C. the stockholders would have received nothing. That is not so. In pretending to determine investment value, P. D. C. disregarded the methods approved by the courts and went on a "frolic of its own." It is elementary that investment value is determined by ascertaining earning capacity, capitalizing the same at an appropriate rate, and deducting the indebtedness (*Consolidated Rock Products Co. v. Du Bois* (1941), 312 U. S. 510; 55 Harv. L. Rev. 125 at 133 (1941); *"The New Schoolmaster in Finance,"* 40 Mich. L. Rev. 625 at 632 (1942)). If the figures of P. D. C. should be accepted (average earnings for twenty-five years after 1948 claimed to have been accurately determined; a 3% rate used because there was practically no risk), the value in 1948 after deducting non-can liabilities was not $3,000,000 but $21,000,000 (Fold. 3, Op. Br. p. 98). As though this were not enough P. D. C. prepared a plan of mutualization which is not a plan of mutualization at all but an option to buy should the stock (on the basis of salvage values) become worth $30,000,000 more than the purchase price and interest. P. D. C. also prepared a trust instrument, as part of the Plan, which deprives appellants of the incidents of the ownership of their stock for thirty-five years.

If, instead of being preoccupied with keeping the management in control, and speculating on a pattern of future earnings and arbitrarily assigning earning figures year by year to perpetuity, P. D. C. had concentrated on trends in the industry and the position of New Company in the industry, and had made appropriate statistical and econ-

PAGE BLEED THRU

omic surveys as to the future interest rate, and had undertaken to estimate earnings for the "foreseeable future," P. D. C.'s estimate of earnings for the first year in the future (*i. e.,* for 1949) would not have been 50% of actual earnings; and when that fact came to light at the hearing before the Insurance Commissioner (Fold. 1, pp. 319 *et seq.*), if P. D. C. had not been stultified by ties of interest with the management, it would have confessed that its entire valuation was a sham; and appellees would not be here suggesting that P. D. C. was generous to the stockholders, without being just to the policyholders, in valuing the stock at $3,000,000 in the face of average actual net earnings for 1953 and 1954 (the last years for which figures are available) of approximately $3,000,000, instead of less than a third that amount, as arbitrarily fixed by P. D. C. [Ex. 28, pp. 9-10]; nor would appellees be here attempting to justify the Plan which contains no unconditional promise to pay, and deprives appellants of the incidents of the ownership of their stock for thirty-five years.

D.

QUESTIONS IMPORTANT AND RECURRING.

In our Jurisdictional Statement we show that, unless the decision of the state supreme court is reviewed on the merits, serious conflicts will result among lawyers, judges, accountants, tax officials and others daily concerned with the valuation of all classes of property both in and out of court; that turnpike promoters and oil and mining operators exercising the power of eminent domain, will be enabled to subject real property to options to purchase for fifty years at the land's present value; that the construction of the mutualization statutes of California, New York, and twelve other states will be placed in doubt; that mutualization as a device for corporate control will

be encouraged; and the unconstitutionality of compulsory mutualization will be thrown in doubt (Juris. State. pp. 46-53).

The only attempt appellees make to meet our argument, if indeed it can be called an attempt, is to assert, by way of *non sequitur*, that a decision of the highest court of a state will not ordinarily be reviewed on the merits unless the questions presented are likely to recur (N. C. p. 32).

CONCLUSION.

Appellees' arguments constitute mere rationalizing. The real reason for the reorganization in 1936, as stated in the majority opinion and by the Insurance Commissioner (Juris. State. p. 10; I. C. p. 8) was that the Commissioner "concluded a plan of reorganization which could not be destroyed by future action or non-action by shareholders was necessary * * *". It has not been denied by appellees that the controlling purpose was not the public good or the benefit of the policyholders, but was the personal aggrandizement of the reorganizers who themselves, as officers of Old Company, were fiduciaries. It plainly appears, also, that the proceedings before the Insurance Commissioner in 1950 were little more than a ritual. It plainly appears, also, that the California courts sacrificed the constitutional rights of appellants on the altar of "polite presumptions."

We urge that the motions to dismiss should be denied.

Respectfully submitted,

JOSEPH L. LEWINSON,
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Attorneys for Appellants.

FRANK E. HOLMAN,
Of Counsel.

February 27, 1956.



DAR

FILED
MAR 2 1956
HAROLD B. WILLEY, Clerk

IN THE

Supreme Court of the United States

OCTOBER TERM 1955

No. 584

FRANK GENTLES, *et al.*, *Appellants*,

v.

F. BRITTON McCONNELL, as Insurance Commissioner of the State of California, *et al.*, *Appellees*.

No. 585

THE PACIFIC MUTUAL LIFE INSURANCE COMPANY OF CALIFORNIA, *et al.*, *Appellants*,

v.

F. BRITTON McCONNELL, as Insurance Commissioner of the State of California, *et al.*, *Appellees*.

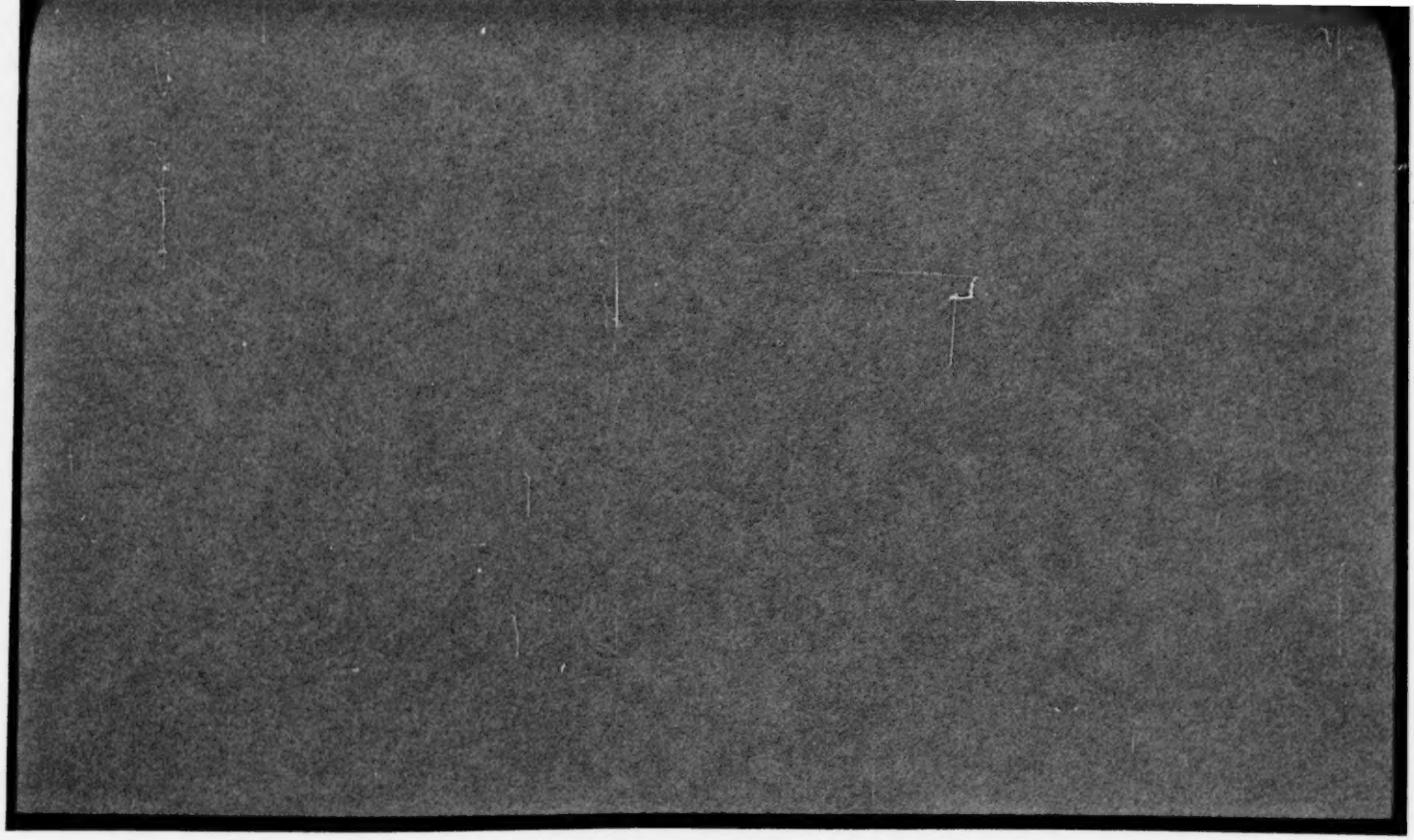
APPEAL FROM THE SUPREME COURT OF THE STATE OF CALIFORNIA

REPLY TO BRIEFS IN OPPOSITION TO MOTION TO DISMISS

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PAGE BLEED THRU



CITATIONS

Cases:

	Page
Carpenter v. *Pacific Mutual Life Ins. Co.*, 10 Cal. 2d 307, 74 P. 2d (76i)	4
Chicago Life Ins. Co. v. *Cherry*, 244 U.S. 25	2
Krier v. *Krier*, 28 Cal. 2d 841, 172 P. 2d 681 (1946)	4
Memphis Gas Co. v. *Beeler*, 315 U.S. 649	3
Neblett v. *Carpenter*, 305 U.S. 297	3, 4, 7
Price v. *South District Agricultural Assn.*, 201 Cal. 502, 258 P. 387 (1927)	4
Ward v. *Love County*, 253 U.S. 17	3

Miscellaneous:

American Jurisprudence, Vol. 30, Judgments, Section 178	4
Developments in the Law—Res Judicata, 65 Harvard Law Review 818	4
Stern, "Separability and Separability Clauses", 51 Harvard Law Review 76	5

IN THE

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APPEAL FROM THE SUPREME COURT OF THE STATE OF CALIFORNIA

REPLY TO BRIEFS IN OPPOSITION TO MOTION TO DISMISS

The briefs in opposition to appellees' motion to dismiss advance only one argument not raised in the jurisdictional statements and discussed in appellees'

motion to dismiss.* The new argument is that the California Superior Court in 1936 did not pass on the provision of the Rehabilitation Agreement by which the Conservator consented in advance to the plan of mutualization contemplated by the Agreement, that in any event the stockholders could not have appealed on that point in 1936, and hence that the court below erred in applying *res judicata* (Br. Opp. No. 584, pp. 7-19). While we hesitate to burden the Court with further papers in this case, we may be warranted in exposing, briefly, the fallacy of appellants' position.

The California Supreme Court explicitly held that "the validity of all portions of the rehabilitation agreement, including the provision for advance consent, is res judicata" (App. A13).** This application of *res judicata* is not, as we pointed out in our Motion to Dismiss, a violation of due process unless it is a mistake "so gross as to be impossible in a rational administration of justice." *Chicago Life Ins. Co.* v. *Cherry*, 244 U.S. 25, 30. No stricter standard is im-

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* Since the jurisdictional question is at the threshold, it may be worthwhile noting that, in our view, the briefs in opposition fall far short of showing that this case is within the appellate jurisdiction of this Court. See N. C. Motion to Dismiss, pp. 11-14. None of the record references cited by appellants show that the validity of the California statutes involved was drawn in question below, and, indeed, appellants' briefs seem almost to concede this point. Moreover, appellants' arguments that the action of the Insurance Commissioner is a "statute" are based largely on state court decisions, despite the fact that appellants in No. 584 recognize that the jurisdictional question "cannot turn on the categories employed by the State courts" (Br. Opp. p. 25).

** The California Supreme Court also held that, apart from *res judicata*, the Conservator's consent in advance to the Plan of Mutualization was valid under California law (App. p. A13).

posed by the cases cited by appellants, (Br. Opp. No. 584, p. 11), for they make it clear that this Court examines non-federal grounds of decision such as *res judicata* only to determine whether they are "plainly untenable" or "so insubstantial as to be in effect an evasion of the constitutional issue." *Ward* v. *Love County*, 253 U.S. 17, 23; *Memphis Gas Co.* v. *Beeler*, 315 U.S. 649, 654.

The holding of the court below that the validity of the provision of the Rehabilitation Agreement for the Conservator's advance consent is *res judicata* has a sound basis. On September 25, 1936, the Insurance Commissioner presented the Rehabilitation Agreement to the California Superior Court for approval. *Neblett* v. *Carpenter*, 305 U.S. 297, 300. The Agreement contained an explicit provision in Section 20(a) that the Conservator "agrees to consent and hereby consents as the holder and owner of the stock of New Company" to the plan of mutualization contemplated by the Agreement (App., p. F27). The Superior Court issued an order "which directed all interested persons to show cause why the Agreement ... should not be approved," and at a "hearing, which lasted from October 19 to December 4 [1936], many officers, stockholders and policy holders" were heard. *Neblett* v. *Carpenter*, 305 U.S. 297, 300.

On December 4, 1936, an order was entered by the Superior Court approving "each and all of the terms and conditions" of the Rehabilitation Agreement and directing the Conservator "fully and faithfully to perform, carry out and discharge each and all of the obligations, terms, conditions and covenants on his part to be performed under the terms" of the Agreement (Ex. 8, Pars. 13 and 15; see *Neblett* v. *Carpenter*,

305 U.S. 297, 300). That order "forever barred and enjoined [all persons] from making hereafter any complaint in respect of the said Rehabilitation and Reinsurance Agreement, or any provision or provisions thereof" (Ex. 8, Par. 22; see App. p. A8). The order was affirmed by the California Supreme Court (*Carpenter* v. *Pacific Mutual Life Ins. Co.*, 10 Cal. 2d 307, 74 P. 2d 761) and ultimately by this Court. *Neblett* v. *Carpenter*, 305 U.S. 297.

Against this background, the court below held that since the same parties or their privies were involved in both proceedings, the validity of every provision of the Rehabilitation Agreement, including the provision for advance consent, is *res judicata* (App. p. A8). The court reasoned that "The basic issue before the Court when the agreement was submitted for approval was the propriety of each of its provisions, and the determination of that issue is conclusive as to every matter which might have been urged to sustain or defeat its determination" (App. p. A9). Far from being "an evasion of the constitutional issue," this ruling is consistent with a long line of prior California decisions, as well as with decisions of other courts. See, *e.g.*, *Price* v. *Sixth District Agricultural Assn.*, 201 Cal. 502, 258 P. 387 (1927); *Krier* v. *Krier*, 28 Cal. 2d 841, 843, 172 P. 2d 681 (1946); 30 Am. Jur., Judgments, § 178; Developments in the Law—Res Judicata (1952) 65 Harv. L. Rev. 818, 840-841.

Appellants argue that the circumstances of this case should have led the court below to refuse to apply *res judicata*. First, they urge that the "separability

clause" in Paragraph 20(f) of the Agreement* somehow "made it unnecessary" for the court in 1936 to determine the validity of the Conservator's advance consent to the plan of mutualization (Br. Opp. No. 584, p. 7). The argument, however, ignores both the language of Paragraph 20(f) and the nature of a separability clause. Paragraph 20(f), like any separability clause, would have become operative only if some provision of Paragraph 20 were held void; that not having occurred, Paragraph 20(f) ceased to have further significance.** We know of no case—and

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* Separability clauses such as Paragraph 20(f) which are directed at a particular section of a contract or statute are increasingly common where the draftsman wishes to leave no doubt as to the separability of a given section and its parts. See Stern, "Separability and Separability Clauses" (1937) 51 Harv. L. Rev. 76, 125-128.

** Appellants' present argument was urged upon and rejected by the Trial Court which said:

> "I think they misconstrued the purpose of subparagraph (f). The purpose thereof was undoubtedly to enable the court in the proceeding had for the approval of Rehab either to approve the plan as a whole, or if it believed certain portions of paragraph 20 to be illegal, then to approve it with those parts deleted. In other words, the petitioners there said to that court: 'We ask you to approve this agreement as a whole, but if you cannot give your approval to it as a whole, we ask you to approve it, after deleting therefrom such portions of paragraph 20 as you find contrary to law.'
>
> "They thus submitted to the court by their petition the validity of all of the terms and conditions of paragraph 20, and when the court gave its approval of the agreement without finding any provision of paragraph 20 to be contrary to law, it, by its judgment, established the validity of each of the provisions of that paragraph, and it became an integral part of the approved agreement; subparagraph (f) had then served its purpose." (App. pp. C17-C18)

appellants cite none—suggesting that a separability clause weakens the effect of a judgment holding all the provisions of an agreement valid, and there is no logical reason why it should do so.

Second, appellants argue that the Conservator's consent in advance was not in issue in the 1936 litigation because of the provisions of Paragraph 25 of the Rehabilitation Agreement. Again the argument misconstrues the Rehabilitation Agreement. Paragraph 25, of which appellants quote only a part,* is entitled "Conservator Not Personally Liable", and it relates solely to that subject. What Paragraph 25 means is that Samuel L. Carpenter, Jr., the Conservator, shall not be personally liable if any action taken by him pursuant to the Rehabilitation Agreement is later successfully attacked. This exclusion of personal liability in Paragraph 25 could not, and did not, obviate the necessity of the court's determining in 1936 the validity of all of the provisions of the Rehabilitation Agreement, including the Conservator's consent in advance.

Third, appellants say that *res judicata* is inapplicable because an attack on the provisions for advance consent would have been held premature by this Court had it been made in the 1936 litigation. This contention,

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* The full text of Paragraph 25 is as follows:

"(25) No personal liability on the part of Samuel L. Carpenter, Jr. is assumed under this agreement, but he is bound by the provisions of this agreement only in his capacity as such Conservator or as Liquidator of the Old Company. All undertakings and obligations herein set forth as undertakings or obligations of the Conservator are made only in his said capacities and to such extent as he had authority to make the same, and the Conservator makes no warranty of his authority to make the same."

however, ignores the fact that the "validity of all of the provisions of the [Rehabilitation] agreement was put in issue by the petition" for its approval, and that the order of the California Superior Court in 1936 held valid "each and all" of said provisions and "forever barred and enjoined" all persons from thereafter attacking any of them, (App., p. A8).* It was open to the parties in that case to assert then, as they now do, that the advance consent of the Conservator was a deprivation of their constitutional rights, and to urge that they could not properly be denied the right to question the propriety of that consent at a later time.** Indeed, the attack upon the Rehabilitation Agreement in *Neblett* v. *Carpenter* itself was made *in limine*, and many of the issues there raised and determined by this Court were likewise related to the possible future effect of the Agreement. As a minimum, and even had this Court deemed the validity of the advance consent provision to be premature, there could have been no doubt as to the right of the parties to urge that the Superior Court's injunction should be modified to permit a later attack on that provision. Appellants' argument on prematurity simply ignores the conclusive character of the 1936 order and seeks to assert now that it did not mean what it plainly said.

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* The terms of the order and of the injunction completely deflate appellants' claim that they were "lulled into security" and that the "courts below have made the Rehabilitation Agreement a trap for the unwary" (Br. Opp. No. 584, p. 9).

** As the California Supreme Court said, "there was nothing to prevent the questions which are raised with regard to the validity of the rehabilitation agreement from being litigated in the proceeding which led to the order approving the agreement." (App. p. A12).

The heart of the matter is that the prior litigation approving all of the provisions of the Rehabilitation Agreement forecloses the basic claim made by appellants in this Court. Appellants indeed concede as much (Br. Opp. No. 584, p. 6), and underscore that fact by their strenuous efforts to avoid the force of *res judicata*. Policyholders, in accepting reinsurance twenty years ago and in purchasing new insurance since that time, have relied on the fact that the Superior Court's order meant what it said in barring all future attacks on any provisions of the Rehabilitation Agreement, including the mutualization option which gave them an opportunity to become owners of the Company. In the 1936 litigation, appellants might have challenged the provisions of the Rehabilitation Agreement binding the Conservator (and, through him, appellants) to consent to the price and terms of payment fixed by the plan of mutualization promulgated in accordance with the terms of the Agreement. They did not elect to make the challenge then; they may not do so now.

Respectfully submitted,

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March, 1956.

No. 585.

MAR 7 195
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In the Supreme Court of the United States

October Term, 1955

THE PACIFIC MUTUAL LIFE INSURANCE COMPANY OF CALIFORNIA, a California corporation, SAMUEL K. RINDGE, and WILLIAM H. JACK,

Appellants,

vs.

F. BRITTON McCONNELL, as Insurance Commissioner of the State of California, F. BRITTON McCONNELL, Insurance Commissioner of the State of California, as Liquidator of The Pacific Mutual Life Insurance Company of California, and PACIFIC MUTUAL LIFE INSURANCE COMPANY, a California corporation,

Appellees.

On Appeal From the Supreme Court of the State of California.

REJOINDER TO REPLY BRIEF.

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SUBJECT INDEX

PAGE

1. The claim as to the advance consent is not a basic one..... 2
2. The point as to the advance consent is cumulative only..... 2
3. New Company's present contention is unsupported by the opinion of the State Supreme Court..... 4

Conclusion 5

TABLE OF AUTHORITIES CITED

STATUTES

Insurance Code, Sec. 11526..... 3

Insurance Code, Sec. 11526(b) 2, 3

Insurance Code, Sec. 11526(c)..... 3

Insurance Code, Sec. 11527..... 3

In the Supreme Court of the United States

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No. 585.

THE PACIFIC MUTUAL LIFE INSURANCE COMPANY OF CALIFORNIA, a California corporation, SAMUEL K. RINDGE, and WILLIAM H. JACK,

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Appellees.

On Appeal From the Supreme Court of the State of California.

REJOINDER TO REPLY BRIEF.

In its Reply Brief New Company says: "The California Supreme Court expressly held that 'the validity of all portions of the rehabilitation agreement, including the provision for advance consent, is res judicata.'" (p. 2.) From this New Company argues: "The heart of the matter is that the prior litigation approving all of the provisions of the Rehabilitation Agreement forecloses the basic claim made by appellants in this Court." (p. 8.) By "the basic claim" New Company means appellants' argument that, by holding the validity of the advance consent was res judicata, the state supreme court deprived appellants of their day in court.

1. The Claim as to the Advance Consent Is Not a Basic One.

This is an appeal from the 1955 judgment of the state supreme court affirming the judgment of the superior court denying a writ of mandate to vacate the 1950 order of the insurance commissioner. The questions presented are whether the order of the insurance commissioner and the judgment of the state supreme court deprive appellants of their property without due process of law for the reasons stated in our Jurisdictional Statement (pp. 4-6). The invalidity of the advance consent is not among the reasons stated.

In our Jurisdictional Statement we devote a line and a half of text (p. 46) and a portion of a twelve line note (p. 16, note 7) to the invalidity of the advance consent. In our Brief in Opposition we devote two pages to showing, in answer to appellees' arguments, that the order of December 4, 1936 could not have been res judicata as to the validity of the advance consent without denying appellants their day in court (pp. 22-23). This is the extent of our treatment of advance consent in the Jurisdictional Statement and Brief in Opposition filed in this Court prior to the filing of New Company's Reply Brief.

Plainly, the point as to advance consent is not a basic one.

2. The Point as to the Advance Consent Is Cumulative Only.

Even though the advance consent were valid, that circumstance would not be controlling here. Indeed, had the Liquidator, after full consideration of the plan, given present consent in 1950, on behalf of the stockholders, under the provisions of §11526(b), still the plan of mu-

tualization would have been waste paper if the insurance commissioner had not approved it under §11526(c), after a full hearing under §11527.[1]

Section 11526 governing voluntary mutualization calls for affirmative action by (a) the directors, (b) the stockholders, (c) the insurance commissioner, and (d) the policyholders. As shown in our Jurisdictional Statement and not denied by any one, the insurance commissioner conceded in the state supreme court that the advance consent given by the Conservator was only the consent called for by subdivision (b); and the consent of the stockholders is not the test of whether the plan satisfies the statutory standard of fairness, but that must be independently determined by the insurance commissioner. (Juris. State. pp. 33-34, note 20.) There was no dispute about either of those propositions before the insurance commissioner or in the state courts. New Company spent three weeks in the 1950 proceeding offering evidence in support of the plan. The insurance commissioner not only heard the evidence, but also explicitly stated that "the approval or disapproval of the Plan by the commissioner is under statutory rather than contract provisions," i.e. was governed by §11527 of the Insurance Code and not the provisions of the Rehabilitation Agreement. (Fold. 1, p. 6.) In reviewing the proceedings the state supreme court dealt with the hearing before the insurance commissioner on the same footing. (Juris. State. p. 15, note 6; Br. in Opp. p. 14.)

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[1]See, Folder three, Op. Br. p. 229.

3. New Company's Present Contention Is Unsupported by the Opinion of the State Supreme Court.

The present argument is but a revised version of the argument made in the motions to dismiss, i.e. the order of December 4, 1936 required the insurance commissioner in the 1950 proceeding to rubber stamp the plan of mutualization and not exercise his own discretion as to its fairness and equity. (Mot. N. C. p. 18; Mot. I. C. pp. 13, 17.) That argument has been shown to be based on the opinion of the appellate court which was repudiated by the state supreme court. (Our Br. in Opp. pp. 13-14.) Appellees have, of course, correctly quoted the statement from the opinion of the state supreme court relative to the validity of the advance consent being res judicata. But it is plain that the state supreme court did not (and could not consistently with due process) have construed the advance consent as limiting the duties of the insurance commissioner in 1950 in passing on the fairness and equity of the plan of mutualization. (Id. pp. 15-21.) As to that proposition New Company raises no question in its latest document.

In its Reply Brief New Company tries to meet our arguments by claiming that the reservations in paragraph 20 became *functus officio* upon the signing of the order of December 4, 1936. We anticipated and met that argument in our Jurisdictional Statement (p. 35) and the insurance commissioner conceded the point in the state courts. (Fold. 3, I. C. Br. p. 62.)

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CONCLUSION.

It is hard to understand why New Company has traveled outside the Rules to reiterate a point that has already been demolished, particularly as the point is not a controlling one, and is of such a minor character as to be merely cumulative. It is, we believe, a measure of the unsoundness of appellees' motions to dismiss that New Company should make an eleventh hour effort to focus attention on non-essentials.

New Company says "appellants" concede their present point (p. 8). New Company cites Br. in Opp. No. 584, page 6. The reference does not bear out New Company. Besides it is not even claimed that appellants in No. 585, including Old Company which is the equitable owner of the stock of New Company, have made any such concession.

It is submitted that the motions to dismiss should be denied.

Respectfully submitted,

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FRANK E. HOLMAN,
Of Counsel.

March 6, 1956.

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MAR 8 1956
HAROLD B. WILLEY,

IN THE

Supreme Court of the United States

OCTOBER TERM, 1955

No. 584

FRANK GENTLES, *et al.*,

Appellants,

—against—

F. BRITTON McCONNELL, as Insurance Commissioner of the State of California, *et al.*,

Appellees.

ON APPEAL FROM THE SUPREME COURT OF THE STATE OF CALIFORNIA

APPELLANTS' MEMORANDUM ANSWERING THE "REPLY" OF APPELLEE PACIFIC MUTUAL LIFE INSURANCE COMPANY

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Attorneys for Appellants.

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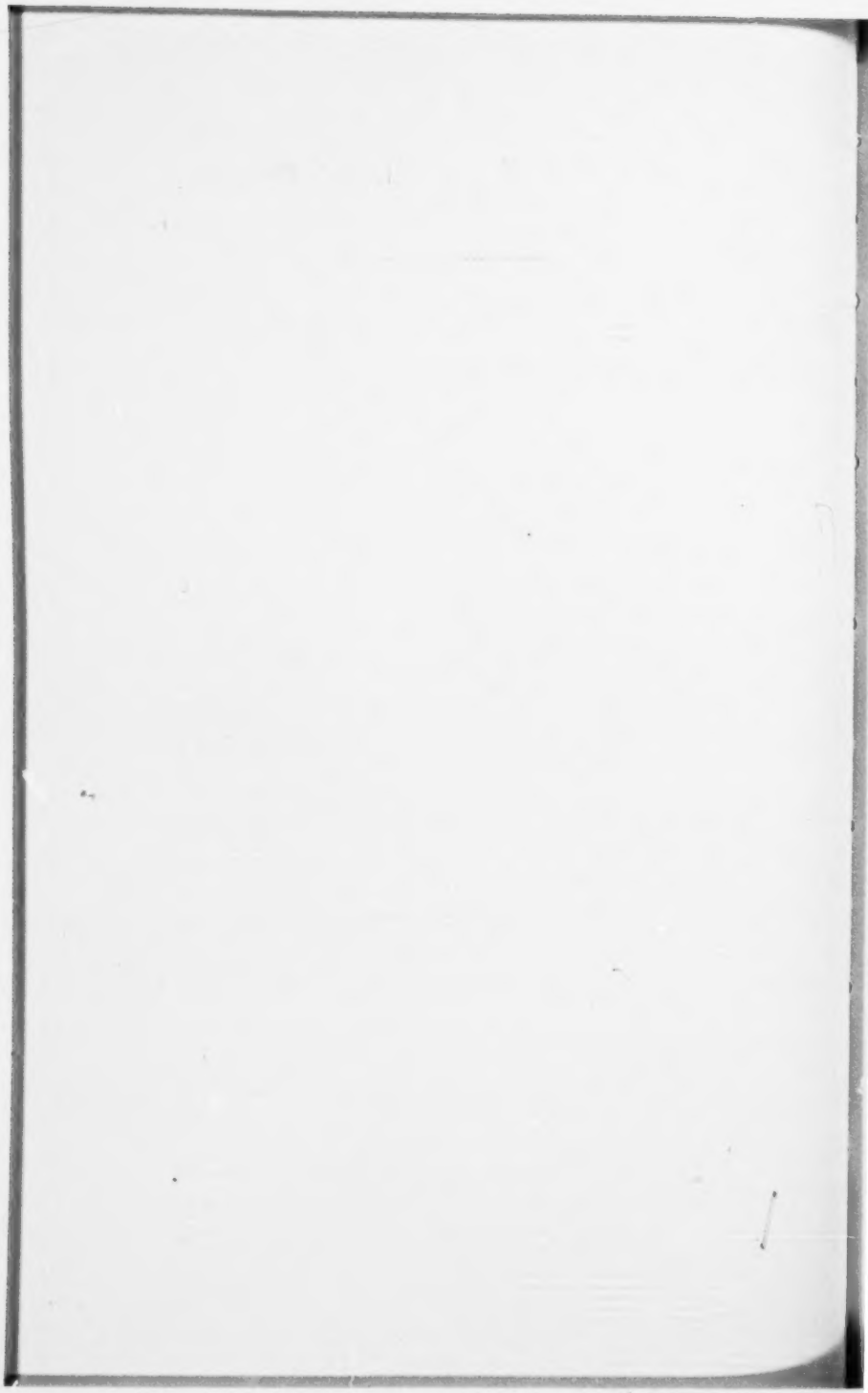


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CITATION

CASE:	PAGE
Neblett v. *Carpenter*, 305 U. S. 297	3, 4

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IN THE

Supreme Court of the United States

October Term, 1955

FRANK GENTLES, *et al.*, *Appellants*, —*against*— F. BRITTON MCCONNELL, as Insurance Commissioner of the State of California, *et al.*, *Appellees.*	No. 584

ON APPEAL FROM THE SUPREME COURT OF THE STATE OF CALIFORNIA

APPELLANTS' MEMORANDUM ANSWERING THE "REPLY" OF APPELLEE PACIFIC MUTUAL LIFE INSURANCE COMPANY

New Company has filed a "Reply" to our Brief in Opposition to Appellees' Motions to Dismiss, and has stated therein (p. 8):

> "The heart of the matter is that the prior litigation approving all of the provisions of the Rehabilitation Agreement forecloses the basic claim made by appellants in this Court. Appellants indeed concede as much (Br. Opp. No. 584, p. 6), and underscore that fact by their strenuous efforts to avoid the force of *res judicata*."

We made no such concession. All we said at page 6 of our Brief in Opposition was that the *res judicata* argument was Appellees' only possible escape from the conclusion that

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Appellants' property has been taken in violation of the 14th Amendment. We then proceeded to show why *res judciata* in fact provided no such escape. (Br. Opp. No. 584, pp. 7-12.)

New Company's statement about "the heart of the matter" asserts a proposition that is plainly untenable. It amounts to arguing that a binding adjudication as to the fairness of a mutualization plan can be had ten years or more before the plan has come into existence. That argument goes far beyond the decision of the court below, which did not apply *res judicata* to the validity of the Commissioner's order approving the plan. Moreover, the argument proves too much. It amounts to saying that the 1936 proceedings so fixed the relationships and rights of all interested parties that, when the Commissioner was subsequently called upon to exercise his statutory function of passing on the fairness of a mutualization plan, his action is immune to *any* form of legal review as to *any* unconstitutional aggrievement such action might have inflicted, or *any* spoliation or injustice that might have ensued from it; and that *any* abdication of his statutory duties must go unquestioned. In fact, it amounts to a claim that our challenge to the Commissioner's order approving the plan of mutualization is not litigable.

The New Company is aware that there is an issue of *res judicata*, affecting Appellants' "basic claim", because at page 7 of its "Reply" it addresses itself to that issue. In attempting to meet our argument that the constitutionality of the advance consent was a question which—because it was premature—could not have been raised in 1936, New Company argues that Old Company stockholders could have raised the constitutional question in 1936 anyway, and

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urged that the 1936 order (which New Company calls "an injunction") be modified so as to reserve for later decision the constitutional issues that might be involved in an attack on that provision. The argument is absurd, since nobody has to give advance notice that he will assert and protect his constitutional rights if and when an infringement of them is attempted. The argument that the 1936 order is conclusive *because it says so* (Reply, pp. 4, 7) begs the question, since constitutional rights cannot be shut off merely by an *assertion*, in the absence of a justiciable controversy.

Other arguments in the Reply are also plainly erroneous, viz.:

1. The New Company argues that it was open to Appellants in 1936 to assert the invalidity of the advance consent of the Conservator, as being a deprivation of their constitutional rights (Reply, p. 7); and for that proposition they cite a portion of the opinion below (Reply, p. 7, fn. **). But that argument begs the question, because a person cannot assert in the abstract that something deprives him of constitutionl rights, but must show *that* he has been deprived—and *how* he has been deprived—of life, liberty or property without due process. See Br. Opp. No. 584, p. 10, fn. **. Moreover, this is particularly so where there could be no way of knowing what the applicable law might be at the time when the request for mutualization might be made. See Br. Opp. No. 584, p. 9, fn. See also App. F-24.

2. New Company profusely cites and quotes from *Neblett* v. *Carpenter*, 305 U. S. 297, in a manner which gives the misleading impression that this Court decided in that case the issues which are being raised in the instant proceeding (Reply, pp. 3-4, 7). But the fact is

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that the Old Company stockholders were not parties to any of the appeals which culminated in this Court's decision in *Neblett* v. *Carpenter, supra*, and any reading of that opinion makes it clear that this Court did not at that time have any of the present issues before it, but was addressing itself to entirely different questions.

3. The New Company's argument with respect to the separability clause in the Rehabilitation Agreement (Reply, p. 6) ignores the fact that the separability clause relates only to the mutualization provisions of the Rehabilitation Agreement. The existence of such a reservation in the context in which it appears leads to a conclusion precisely contrary to that urged by the New Company. The inclusion of the separability clause in the mutualization provisions establishes that the issues to which it applies remain open for future litigation. Therefore, any finding as to the validity of the advance consent was not necessary to sustain the 1936 order of the Superior Court. No citation of cases is required for the established proposition that findings which are not necessary to sustain a judgment, or to reach a decision, are not *res judicata* in any future litigation.

The superficiality of New Company's position on *res judicata* clearly appears in the final sentences of its Reply (p. 8):

> ". . . Policyholders, in accepting reinsurance twenty years ago and in purchasing new insurance since that time, have relied on the fact that the Superior Court's order meant what it said in barring all future attacks on any provisions of the Rehabilitation Agreement, including the mutualization option which gave them an opportunity to become

owners of the Company. In the 1936 litigation, appellants might have challenged the provisions of the Rehabilitation Agreement binding the Conservator (and, through him, appellants) to consent to the price and terms of payment fixed by the plan of mutualization promulgated in accordance with the terms of the Agreement. They did not elect to make the challenge then; they may not do so now."

We are not arguing that policyholders, who accepted reinsurance in, or purchased new insurance from, New Company are not entitled to exercise the option to mutualize. But it does not follow from this that these policyholders, in the exercise of this option, are entitled to have the State of California take Appellants' property at a confiscatory price for their benefit. We are not attacking "the mutualization option" in the Rehabilitation Agreement. We are attacking the Plan of Mutualization and we are attacking the procedures by which this plan, though confiscatory, has been held to be fair and equitable, without a procedurally fair administrative or judicial hearing. We are claiming that we are not foreclosed from demanding a fair and equitable plan, and procedurally sufficient hearing and judicial review, by anything that was approved by the Superior Court in 1936.

Respectfully submitted,

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ALAN Y. COLE,
Of Counsel.

March 8, 1956.

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APR 23 1956

HAROLD B. WILLEY, Clerk

IN THE

Supreme Court of the United States

October Term, 1955

Nos. 584 and 585

THE PACIFIC MUTUAL LIFE INSURANCE COMPANY OF CALIFORNIA, a California corporation, FRANK GENTLES, DON F. GATES, RANDOLPH CALDWELL, FRANCIS V. NIXON, SAMUEL K. RINDGE, and WILLIAM H. JACK, *Petitioners,*

v.

F. BRITTON MCCONNELL, as Insurance Commissioner of the State of California, F. BRITTON MCCONNELL, Insurance Commissioner of the State of California, as Liquidator of The Pacific Mutual Life Insurance Company of California, and PACIFIC MUTUAL LIFE INSURANCE COMPANY, a California corporation, *Respondents.*

CONSOLIDATED PETITION FOR REHEARING

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INDEX

	Page
Preliminary Statement	2
Statement	2
Reasons for Granting the Rehearing	6
1. The Question of Confiscation	6
2. The Question of Judicial Review	17
3. Res Judicata	20
Conclusion	21

TABLE OF CASES

CASES:

Alabama Public Service Commissioner v. Southern R. Co., 341 U.S. 341 ..... 17, 19
American Trucking Assoc. v. United States, 344 U.S. 298 17
Bailey v. Minsch, 168 F. 2d 635 16
Baltimore & Ohio R. Co. v. United States, 345 U.S. 146 17
Bondholders Inc. v. Powel, 342 U.S. 921 18
Buchanan v. Warley, 245 U.S. 60 8
Consolidated Rock Products Co. v. DuBois, 312 U.S. 510 16
Ecker v. Western Pac. R. Corp., 318 U.S. 448 ... 16, 17, 18
Brief of Solicitor General, 87 L. Ed. 918 18
Re Equitable Office Building Corporation, Debtor, 96 L. Ed. 1386 18
FPC v. Hope Natural Gas Co., 320 U.S. 591 19
General Stores Corp. v. Shlensky, — U.S. —. 24 Law Week 4141 18
International Harvester Corp. v. Goodrich, — U.S. —, 24 Law Week 4183 ..... 9, 14
Monongahela Nav. Co. v. U. S., 148 U.S. 312 16
Niagara Hudson Corp. v. Leventritt, 340 U.S. 336 .. 17
Ohio Valley Water Co. v. Ben Avon Borough, 253 U.S. 287 ..... 18, 19

Page

Old Dearborn Co. v. Seagram Corp., 299 U.S. 183 .. 8
Otis & Co. v. SEC, 323 U.S. 624 16
RFC v. Denver and Rio Grande Western R. Co., 328 U.S. 495 17
St. Joseph Stockyards Co. v. United States, 298 U.S. 38 19
SEC v. Central-Illinois Corp., 338 U.S. 96 17
SEC v. Central-Illinois Corp., supra, Comments of Justice Rutledge 18
Shelley v. Kraemer, 334 U.S. 1 6
State Corp. Comm. v. Wichita Gas Co., 290 U.S. 561 18
Thompson v. Consolidated Gas Co., 300 U.S. 55 ... 9
United Railways & Electric Co. of Baltimore v. West, 280 U.S. 234 18
United States v. Miller, 317 U.S. 369 14

STATUTES:

28 USC § 1257 (2), (3) 6

MISCELLANEOUS:

Constitution of the United States, Amendment 14 .. 6, 8, 9, 13, 14, 18
Jaffe, Administrative Law (1953) 19
Jurisdictional Statement 584 .....3, 4, 6, 10, 11, 14, 15
Jurisdictional Statement 585 .....3, 4, 6, 15
57 Yale L. J. (1948) 19

IN THE

Supreme Court of the United States

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THE PACIFIC MUTUAL LIFE INSURANCE COMPANY OF CALIFORNIA, a California corporation, FRANK GENTLES, DON F. GATES, RANDOLPH CALDWELL, FRANCIS V. NIXON, SAMUEL K. RINDGE, and WILLIAM H. JACK, *Petitioners,*

v.

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CONSOLIDATED PETITION FOR REHEARING

This is a consolidated petition for rehearing filed on behalf of all of the appellants-petitioners in Nos. 584 and 585, who had filed separate Jurisdictional Statements from a decision of the Supreme Court of the State of California.

Petitioners pray that this Court grant rehearing of its order of March 12, 1956, in these cases.

Orders were granted by Justice Douglas on March 29, 1956, in No. 584, and on April 2, 1956, in No. 585,

extending the time in which to file petitions for rehearing to and including April 26, 1956.

PRELIMINARY STATEMENT

Because these cases were originally presented to this Court as an appeal from the Supreme Court of the State of California, certain aspects of the decisions below so occupied the forefront of the presentation that the importance of certain other aspects of the decisions may have been obscured or overshadowed. Moreover, since respondents-appellees filed motions to dismiss, much space in the papers was devoted to questions relating to this Court's appellate jurisdiction. This petition for rehearing is devoted principally to questions which, we believe, make these cases particularly appropriate for the exercise of this Court's certiorari jurisdiction, and which may not have been adequately presented because the emphasis in the Jurisdictional Statements and subsequent papers was directed towards supporting an appeal.

STATEMENT

This case is the culmination of approximately two decades of litigation arising from the seizure in July, 1936, of the Pacific Mutual Life Insurance Company of California by the California Insurance Commissioner. Detailed statements of the facts have been set out in the Jurisdictional Statements heretofore filed, and to avoid repetition, we include here only a capsuled summary.

In 1936, when the Old Company was declared technically insolvent because its reserves were considered to be inadequate, the California Insurance Commissioner was appointed Conservator (in 1937, he was also ap-

pointed Liquidator) and authorized to carry out a rehabilitation and reinsurance program, all under the aegis of the California courts. The rehabilitation plan called for the organization of a New Company to take over the assets and business of the Old Company. (App. F)[1] The New Company also assumed all of the liabilities of the Old Company except those growing out of the non-cancellable accident and health policies (non-cans), which were assumed upon a scaled-down basis. In exchange, the New Company's capital stock was to go to the Liquidator in trust for all interested persons, including the stockholders of the Old Company. (J. S. 585, pp. 6-8)

Among the many provisions of the rehabilitation plan, was one authorizing voluntary mutualization of the New Company. (App. F 24-31) This provision established a procedure by which, after July, 1946, the New Company could be mutualized. The machinery could be set in motion by requests from ten percent (10%) of the participating policyholders of the New Company; thereafter an Appointing Committee would be constituted which would in turn designate a Price Determination Committee composed of persons skilled in insurance company valuation. The Price Determination Committee would then determine whether mutualization could be practicably accomplished and if so, the proper price to be paid for the stock of the New Company and the terms of payment. The rehabilitation plan also provided that any mutualization plan promulgated pursuant to the procedures it established

[1] All references to Appendix are to the Appendix in No. 584. References to Jurisdictional Statements are indicated by "J. S." followed by the case number. All other references will be specifically described.

was to be submitted "in accordance with the laws of the State of California in effect at the time". (App. F 24)

The procedure established in the rehabilitation plan was put into effect, and the Price Determination Committee was appointed in January, 1947. In April, 1950, this Committee reported that mutualization was practicable and submitted a plan of mutualization. (App. G 1-3) It is this plan of mutualization, and the limitations imposed by the State of California upon any review of this mutualization plan which is the subject of the present dispute.

After the plan was reported, it was submitted to the Insurance Commissioner for his approval pursuant to the laws of California "in effect at the time" which required that he determine whether it would be "fair and equitable in its operation"[2] A hearing was held before the Commissioner at which oral and documentary evidence was taken, and thereafter, the Commissioner issued an opinion and decision approving the plan and holding that it would be fair and equitable in its operation. (App. D)

In November, 1950, the Old Company and some of its stockholders filed a petition for a writ of mandate in the Superior Court naming as respondents the New Company and the Commissioner, both in his capacity as Commissioner and as Liquidator of the Old Com-

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[2] This was done pursuant to the provisions of the California Insurance Code relating to voluntary mutualization. (App. E 11-12) As appears in the Jurisdictional Statements (J. S. 584, pp. 36-39; J. S. 585, pp. 8-10, 52-53) petitioners contend that the involuntary mutualization provisions (App. E 1-9) should have been followed.

pany. The purpose of the suit was to procure a review of the mutualization plan and to have it set aside as confiscatory. (App. C 19, 22, 27) While the Court made elaborate findings, these findings were, as stated by the Judge himself, in effect nothing but conclusions of law. (App. C 13, 14) He limited his inquiry to whether the Price Determination Committee had "acted arbitrarily" and having concluded that it had not, affirmed the Commissioner's decision because the Commissioner could not say that the Committee "acted without reason, and * * * the Commissioner * * * [could not] substitute his * * * reasoning for that of the Committee." (App. C 34) On appeal, the District Court of Appeal affirmed, restating the view that neither the Insurance Commissioner nor the Superior Court was compelled to render any independent judgment as to the fairness of the mutualization plan, but that the determination of the Price Determination Committee was sufficient of itself to support the mutualization plan. (App. B 22-25)

The Supreme Court of California, by a vote of four to three, and with three separate opinions, affirmed the judgment, but on grounds different than those stated by the District Court of Appeals. (App. A)

The Old Company and the stockholders who had challenged the mutualization plan in the California courts filed appeals in this Court. On March 14, 1956, this Court granted motions to dismiss the appeals and, treating the papers whereon the appeals were taken as petitions for certiorari, denied certiorari.

At the outset, and before reaching the Questions Presented, comment seems appropriate concerning the type of state action involved in this case. In the papers heretofore filed, contentions and counter-con-

tentions were made as to whether the action of the Insurance Commissioner in approving the mutualization plan was legislative, quasi-legislative or executive in character. (J. S. 584, pp. 22, 41; J. S. 585, pp. 6, 14, 32-37, 37-41, 42-46, 50, 52; Br. in Opp. 584, pp. 19-24) This issue was relevant, however, only with respect to whether this Court had jurisdiction over the appeals under 28 U.S.C. § 1257(2). It is entirely mooted where the case is presented by certiorari, under 28 U.S.C. § 1257(3). All that is necessary is that the action complained of be state action—of whatever nature—and that rights claimed under the Federal Constitution have been denied. Or, as this Court stated in *Shelley* v. *Kraemer*, 334 U.S. 1, at 14:

> "the [Fourteenth] Amendment makes void 'State action of every kind', which is inconsistent with the guaranties therein contained, and extends to manifestations of 'State authority in the shape of laws, customs, or judicial or executive proceedings' ".

It is clear that, from the very inception of this case when the Old Company was declared technically insolvent, to the final steps when the state courts sustained the Commissioner's approval of the plan of mutualization, the action involved has been state action, in one form or another, and as such is, of course, subject to the limitations of the Fourteenth Amendment.

REASONS FOR GRANTING THE REHEARING

1. The Question of Confiscation

The mutualization plan formulated by the Price Determination Committee and approved by the State Insurance Commissioner and the courts below is remark-

able because it establishes a form of conditional taking and conditional payment which, to our knowledge, has never before been attempted, let alone approved, by any court, state or federal.

A. The mutualization plan provides for a price of $3,000,000 plus simple interest from December 31, 1948, to the date of payment. The time for effecting mutualization is extended to December 31, 1983, and it is provided that mutualization cannot occur unless three conditions are first met.[3] The mutualization plan leaves unanswered two critical questions: will mutualization ever occur; and if so, when will it occur? All that is certain is that *if* mutualization is to take place it must be prior to 1984. And during the waiting period, the stock of the New Company is turned over to Voting Trustees who may not necessarily operate New Company in the best interests of the Old Company or the Old Company stockholders. (App. G 16)

In short, stripped of all the complicated trimmings, the first and most obvious result of the mutualization plan is that the property of the Old Company and its stockholders has been subjected to a 35 year option,

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[3] The three conditions are: (1) the non-can benefits must be fully restored; (2) the New Company's capital and surplus, and a Special Fund created out of the New Company's Participating Department, must at least equal the purchase price with interest; and (3) the surplus (after paying for the stock) must still be at least the sum of (a) four percent (4%) of the New Company's admitted assets, plus (b) twenty-five percent (25%) of premiums collected during the previous year on all group insurance written one a one year term basis, and (c) twenty-five percent (25%) of premiums collected during the previous year on all accident and health insurance.

The significance of these conditions, translated into specific terms in dollars, is discussed in detail in J. S. 584, pp. 23-25, 27-29.

for which no compensation whatsoever has been or will be paid.

The Old Company and its stockholders have been deprived of the ordinary right of a property owner to determine when he will sell and for how much—a right that is "property" within the protection of Amendment XIV. See *Old Dearborn Co.* v. *Seagram Corp.,* 299 U.S. 183, 192; *Buchanan* v. *Warley,* 245 U.S. 60, 74. They have been deprived of the right to raise money to pay off the non-cans and redeem their equity, or to get back their property when the non-cans shall have been paid off. (App. F 29-30) Control of the stock of the New Company will be turned over to Voting Trustees operating under a trust agreement established by the mutualization plan; and thus petitioners will be deprived of the benefits of the trust (with the Conservator as trustee) which the statute created for the protection of all interests, including theirs.[4] (App. C 22-23, 25)

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[4] The stockholders have also been deprived of one of the most important safeguards provided for them in the Rehabilitation Agreement—that the New Company must follow a policy of writing at least fifty percent (50%) of its life insurance as non-participating insurance. (App. F 30, 31) The stockholders derive no benefit from the participating insurance, since the Rehabilitation Agreement set up the Participating Department as if it were a separate mutual company. Therefore, the New Company could completely defeat the interests of stockholders, postpone the date of purchase of the stock and keep the purchase price down by writing more participating and less non-participating insurance. The provisions of the Plan of Mutualization affecting this point are so outrageously watered down that the stockholders are practically without protection against such a course by the New Company. (App. G 12-13)

Whether such a deprivation of the use of property constitutes a "taking" subject to the due process limitations of the Fourteenth Amendment is a substantial question of federal law not heretofore decided by this Court. It is important, not only because it is a constitutional question, but also because it can arise in both state and federal courts in myriad instances. It is a question which is obviously of importance in the field of eminent domain. For example, turnpike planners could subject property adjoining the turnpike to an option to purchase during a 35 year period, exercisable only in the event that traffic conditions required enlarging the capacity of the road. And if the decisions below approving the mutualization plan stand, the turnpike authority would not be compelled to pay any compensation for this 35 year option although it is an encumbrance on the land as real as any easement. And the same problem arises where, as here, a public body seeks to give to one private group rights in or to property which belongs to another private group. *Cf. Thompson* v. *Consolidated Gas Co.,* 300 U.S. 55, 78-80 and cases cited. See also Frankfurter, J., dissenting, in *International Harvester Corp.* v. *Goodrich,* — U.S. —, — (April 9, 1956), 24 Law Week 4183.

If an option to take, imposed by a public body, constitutes in itself a taking, it is obvious that this Court would strike it down unless provision was made for fair compensation. Yet, at the risk of repetition, but to avoid confusion, it should be noted that the $3,000,000 purchase price established by the Mutualization Plan was not as payment for this option to take, but was rather the payment to be made in the event the option is exercised. (App. G 2) *There is no payment whatsoever provided for the 35 year option.*

We believe that the question raised with regard to the validity of this 35 year option without payment imposed by the mutualization plan alone justifies plenary consideration in these cases.

B. In the event that sometime before 1984, the conditions precedent to mutualization are met and mutualization does occur, the mutualization plan provides for the payment to Old Company and its stockholders of the sum of $3,000,000 plus interest from December 31, 1948, to the date paid.[5] (App. G 5, 6) In the establishment of this figure as the purchase price of the New Company (which is the sole property of the Old Company and its stockholders by virtue of their equitable ownership of the New Company stock),[6] there arise a number of questions relating to valuation which are so fundamental and novel as to require some expression and direction from this Court.

The purchase price of $3,000,000 provided for in the mutualization plan was arrived at by the Price Determination Committee in approximately the following manner:

(a) By computing the pattern of earnings of the New Company through the year 2000. (Ex. 28, p. 8, and J. S. 584, Chart II)

(b) By estimating how much of these earnings would be available for restoration of the non-cans. (Ex. 28, p. 8)

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[5] There is also a provision for augmentation in the amount of $250,000 per year for each year by which the full restoration of the non-cans precedes December 31, 1973. (App. G 6).

[6] The first $560,000 of the purchase price may be payable to creditors in liquidation of unpaid interest claims. See Transcription of Hearing Before the Insurance Commissioner, page 885.

(c) By determining, after matching the conclusions in (a) and (b) above, that the non-cans would be fully restored some time between 1971 and 1974. (Ex. 28, p. 8)

(d) By computing the value of the New Company's earnings until perpetuity and excluding the earnings from 1948 through 1974, since these earnings would go to restoration of the non-cans. (Ex. 28, p. 8, and J. S. 584, Charts I and II)

(e) By estimating how much of the earnings from 1974 to perpetuity would be available as dividends to stockholders. (Ex. 28 and J. S. 584, Chart II)

(f) By determining the 1974 value of those earnings available to stockholders to be $27,700,000, and hence the 1974 value of the New Company. (J. S. 584, Charts I and II)

(g) By discounting the 1974 value of the New Company back to 1948 at a ten percent (10%) compound rate, thereby arriving at the $3,000,000 1948 value. (Ex. 28, p. 2, 8, 12)

We make no challenge to the competence of the Price Determination Committee. Nor, for purposes of this petition, do we challenge the methods, techniques, or computations of the Price Determination Committee, with one single, but very important exception.

The 1974 value for the New Company found by the Price Determination Committee is $27,700,000. With this figure we have no present dispute. But this 1974 value was then "discounted" to establish a 1948 price. And this operation works the confiscation which goes to the very heart of this case.

A discount makes sense and has validity only when taken as consideration for the present payment for a future value. The fundamental vice inherent in the approach of the Price Determination Committee is that, though it discounts a future value presumably for a present payment, it does not actually provide for any present payment, but only for a payment some time in the future. There is, therefore, no validity to the so-called discounting of the 1974 value to 1948 because nothing was to be paid in 1948.

That the 1948 price of $3,000,000 so derived will be augmented by interest to the date paid does not cure this deficiency. The 1974 value was discounted at a compound interest rate of ten percent (10%) to procure the 1948 price, but the interest which the plan provides is to be added to the 1948 price is only at an approximate two and one-half percent (2½%) simple rate. (App. G 6) There is a substantial discrepancy between the ten percent (10%) compound rate back to 1948 and the two and one-half percent (2½%) simple interest rate forward from 1948. Consequently, the augmentation of the purchase price by interest does not make an otherwise invalid "discount" valid, for the interest rate employed to augment the 1948 price is not the same interest rate used to procure the 1948 price.[7]

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[7] We do not contend that any particular interest rate is or is not valid or appropriate in this case. We do contend, and most forcefully, that the interest rate used to augment the 1948 price to the date paid be at least comparable to the interest rate used to discount future earnings to derive the 1948 price. For, it must be remembered, that nothing was ever really "taken" in 1948, and nothing was ever paid for, or could be paid for, in 1948.

A single example suffices to make graphic the confiscatory nature of the arrangement in this case: Assume that the mutualization plan will become effective in 1974. By the Price Determination Committee's own calculations, the 1974 value of the New Company will be $27,700,000. But, by using the 1948 purchase price ($3,000,000) and adding to it simple interest at two and one-half percent (2½%), petitioners will receive in 1974 only $4,875,000, approximately $22,825,000 less than the value which the Price Determination Committee itself determined as the 1974 value. If there was ever a more glaring instance of property taken without just compensation within the meaning of the Fourteenth Amendment, we—like Justice Carter below (App. A 64)—have not heard of it.

The fact of the matter is that anybody would buy the stock of any company, anywhere, at any time, on the basis of the formula established by the Price Determination Committee; and nobody, anywhere, at any time, would sell on the basis of the formula established by the Price Determination Committee.

In conclusion, petitioners desire to make it clear to the Court that we are not complaining about the competence of the Price Determination Committee or the value established by the Committee for the New Company's stock in 1974. But we do complain strenuously that we are not getting that value.

Even assuming that the Insurance Commissioner and the courts below were correct in finding that the Price Determination Committee's conclusions as to value were appropriately supported by the evidence, and assuming further that they were not required to make an independent re-appraisal of these conclusions (See Part 2, *infra*), it does not follow that the

$3,000,000 purchase price fixed by the Committee should also have been sustained, since this price *on the face of the record* is not consistent with the value which the Committee had ascertained. There is no support in the decisions of this Court for a procedure where, in the taking of property, the *price* to be paid is many times less than the *value* which the property is determined to have.[8] The Fourteenth Amendment requires that when one man's property is taken and given to another, the requirements of the due process clause must be met, cf. Frankfurter, J., dissenting, in *International Harvester Credit Corp.* v. *Goodrich, supra,* and due process does not permit the substitution of a strangely derived price for a carefully derived value. The decisions below, in sustaining this departure from the accepted and usual course of judicial procedure, clearly call for an exercise of this Court's supervisory jurisdiction.

C. The confiscation resulting from this utilization of substantially different interest rates is made even worse by other features of the plan. For reasons developed at length in our Jurisdictional Statements, the interest established on the $3,000,000 purchase price is itself confiscatory (J. S. 584, pp. 29-30), and the pro-

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[8] ". . . just compensation . . . means the full and perfect equivalent in money of the property taken. The owner is to be put in as good position pecuniarily as he would have occupied if his property had not been taken . . . courts early adopted, and have retained, the concept of market value. The owner has been said to be entitled to the 'value,' the 'market value,' and the 'fair market value' of what is taken. The term 'fair' hardly adds anything to the phrase 'market value,' which denotes what 'it fairly may be believed that a purchaser in fair market conditions would have given,' or, more concisely, 'market value fairly determined.' " *United States* v. *Miller,* 317 U. S. 369, 373-374.

visions for augmentation of the purchase price in the event of the early restoration of non-cans results in extraordinary windfalls to the New Company (J. S. 584, pp. 30-33). We do not further discuss these matters in this petition, but will expand them in the event review is granted.

There is one other feature of the mutualization plan which, we believe, does require comment in this petition. This relates to the operation of the conditions precedent which are required to take place before mutualization can occur. For various reasons set out in detail in the Jurisdictional Statements, (J. S. 584, pp. 27-28; J. S. 585, pp. 5, 12) as a practical matter, before mutualization can occur, the stockholders' equity in the New Company must reach a value substantially in excess of the $3,000,000 purchase price, plus interest, established in the mutualization plan. So—and this is so extraordinary that it prompts disbelief—the Price Determination Committee has, in fact, proffered this proposition to the Old Company and its stockholders: 'Any time within the next 35 years if the New Company (which you own) achieves a value far in excess of $3,000,000 you will receive $3,000,000 for it, but if it does not achieve this value in 35 years, then our deal is off; in the meantime, we will arrange that during those 35 years the New Company will be run for you, but not necessarily in your best interests; and during this 35 year period you cannot buy your company back at any price.'

We believe that the mere statement of this proposition is sufficient and that no argument is necessary.

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The unique and novel features in the mutualization plan can be employed in any instance in which there is need to develop a present price for a going concern, based upon its future earnings. It may thus be used not only in other insurance mutualizations, but in corporate reorganization proceedings as well. Can stockholders in reorganization cases, for example, be forced to accept a conditional obligation for the capitalized present value of their stock when such obligation bears two and one-half percent (2½%) simple interest, and at the same time the present value of future profits have been determined by discounting the future profits on a ten per cent (10%) compound interest basis?[9]

If this plan, which has been held to be "fair and equitable" (App. D 22) is permitted to stand without review by this Court, its techniques can be used in other arrangements where the test is also "fair and equitable"; *Consolidated Rock Products Co.* v. *DuBois*, 312 U.S. 510 (Bankruptcy); *Ecker* v. *Western Pac. R. Corp.*, 318 U.S. 448 (Railroad Reorganization); *Otis & Co.* v. *SEC*, 323 U.S. 624 (Public Utility Holding Company Act); *Bailey* v. *Minsch*, 168 F. 2d 635 (1 Cir., 1948) (Receivership) cert. den., 335 U.S. 854; and, indeed, in any instance in which a taking of property requires a determination of present value based on future profits. *Cf. Monongahela Nav. Co.* v. *U. S.*, 148 U.S. 312, 336-337 (toll franchise).

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[9] And this, when the obligation to pay stockholders is dependent upon the same contingency as the emergency of future profits?

2. The Question of Judicial Review

In addition to the questions relating to confiscation, this case also poses another substantial constitutional question of widespread importance as to the scope and extent of judicial review in a valuation case where confiscation is claimed.

There is no dispute that the fairness and equity of the mutualization plan was at no time subjected to independent examination by any judicial tribunal in this case. The form of review afforded by the courts below was at best the substantial evidence test. Yet, the decisions of this Court have held that where a property owner claims that his property is being confiscated by forced disposal for less than it is worth, he is entitled to a genuine and full judicial review, the only restriction being that no new evidence may be introduced before the reviewing court. *Alabama Public Service Commission* v. *Southern R. Co.*, 341 U.S. 341, 348-50; *American Trucking Assos.* v. *United States*, 344 U.S. 298, 320-322; *Baltimore & Ohio R. Co.* v. *United States*, 345 U.S. 146.

So far as counsel can determine, this Court has sanctioned the use of the substantial evidence type of review in corporate reorganization involving property valuations in only two special situations, namely, ICC railroad reorganizations and SEC public utility holding company simplifications. *Ecker* v. *Western Pac. R. Corp.*, 318 U.S. 448; *RFC* v. *Denver and Rio Grande Western R. Co.*, 328 U.S. 495, *SEC* v. *Central-Illinois Corp.*, 338 U.S. 96, *Niagara Hudson Corp.* v *Leventritt*, 340 U.S. 336. It is hardly necessary to point out that the present case involves no issues of public urgency, no "brigading" of court and highly expert

administrative agency, and no circumstances of any kind comparable to those which persuaded this Court to permit the ICC and SEC exceptions. Cf. *Ecker* v. *Western Pac. R. Corp., supra,* at p. 468.

The importance of guidance from this Court on this difficult and critical question of judicial review has frequently been noted. See Brief of Solicitor General in *Ecker* v. *Western Pac. R. Corp., supra,* reported at 87 L. Ed. 918, 920; similar comments of Justice Rutledge in *SEC* v. *Central-Illinois Corp., supra,* at 113 *et seq.* See also Justice Frankfurter's special opinion in connection with denial of certiorari in *Bondholders Inc.* v. *Powell,* 342 U.S. 921; and Justice Reed's special opinion on application for stay in re *Equitable Office Building Corporation, Debtor,* 96 L. Ed. 1386 (not officially reported). And as recently as March 26, 1956, this Court reaffirmed its traditional concern in monitoring the form of proceeding required in the overhauling of financially distressed businesses. *General Stores Corp.* v. *Shlensky,* — U.S. —, 24 Law Week 4141.

The basic problem in this case stems from *Ohio Valley Water Co.* v. *Ben Avon Borough,* 253 U.S. 287, where this Court held that the Fourteenth Amendment required that, in all cases where a state administrative order is attacked as confiscatory, "the state must provide a fair opportunity for submitting that issue to a judicial tribunal for determination upon its own independent judgment as to both law and facts", 253 U.S. at 289. The doctrine promulgated in this case was expressly followed in two later cases—*United Railways & Electric Co. of Baltimore* v. *West,* 280 U.S. 234, and *State Corp. Comm.* v. *Wichita Gas Co.,* 290 U.S. 561. Thereafter, the *Ben Avon* doctrine was

clarified and somewhat narrowed in *St. Joseph Stockyards Co.* v. *United States,* 298 U.S. 38. See particularly 298 U.S. at 49-54.

Since the *St. Joseph* decision, the *Ben Avon* doctrine has not been expressly applied by this Court. Indeed, some commentators have speculated that it no longer has vitality. See *Note* 57 *Yale L. J.* (1948) 639 and authorities cited in fn. 1; *Cf. Jaffe, Administrative Law* (1953) p. 617. Undoubtedly, the doctrine has been limited in its effectiveness by the increasingly narrow application of substantive due process in the economic field. *Cf. FPC* v. *Hope Natural Gas Co.,* 320 U.S. 591. And although this Court has not expressly applied the *Ben Avon* doctrine since 1937, there has been some recognition of its continuing validity in a recent case. Frankfurter, J., concurring in *Alabama Public Service Commissioner* v. *Southern R. Co.,* 341 U.S. 341, 362.

The majority of the Court below held that independent judicial examination was not required (App. A 14) and Justice Carter, dissenting, stated that in his view this denial worked a deprivation of due process under the federal constitution, citing, *inter alia,* the *Ben Avon* and *St. Joseph Stockyard* cases. (App. A 56-64) Moreover, the importance of this principle in this case is more than abstract, since the trial judge expressly stated that if he had been able to make an independent examination and judgment he "could not take the facts and arrive at the same conclusion; not by a long shot." (App. A 65)

Thus, this case provides a direct and meaningful opportunity to re-examine the *Ben Avon* doctrine in the light of modern trends and the increase in administrative regulation, and to set at rest—as only this Court

can—the questions of whether the doctrine continues to apply today and, if so, the precise scope and extent of its application.

3. Res Judicata

Much has been written in the decision below and in the papers filed in this Court by respondents-appellees regarding the application of the doctrine of res judicata. In fact, the gist of respondents-appellees' arguments have been that all [redacted] contentions are foreclosed by res judicata (see Appellants' Memorandum, No. 584, p. 2).

We do not desire, in this petition, to re-argue at any length this issue of res judicata. For present purposes, it is sufficient to state that the questions presented under points 1 and 2, *supra,* are plainly outside the scope of any and all claims of res judicata made by respondents-appellees.

The doctrine of res judicata necessarily presupposes a prior occasion in which issues were or could have been litigated between the same parties. Neither the claim of confiscation directed at the substance of the mutualization plan, nor the denial of appropriate judicial review in the state courts of California were or could have been litigated until the instant proceeding was instituted. Consequently, res judicata is plainly inapplicable to them. This litigation, after all, was instituted solely to challenge and procure a review of the substance of the mutualization plan itself. No prior litigation could be res judicata with regard to the validity of the mutualization plan because there was no mutualization plan heretofore. Similarly, the question of judicial review in the California courts could not have been raised heretofore, because *this* is

the case in which that judicial review based on confiscation was first demanded.

And, there is still another important reason why any claim of res judicata cannot be properly made against the points asserted in this petition. This is because Paragraph 20(a) of the Rehabilitation Agreement—which is the seed from which respondents-appellees' claims of res judicata stem—expressly provides that the mutualization plan, when formulated, must be submitted "in accordance with the laws of the State of California in effect at the time." (App. F 24) To put it in its simplest terms, it would have been impossible at the time the Rehabilitation Agreement was approved in 1936 to know, and therefore to litigate, what laws of the State of California relating to mutualization would be in effect in 1950.

CONCLUSION

For the reasons set forth above, and in the papers heretofore filed in these cases, it is respectfully submitted that a rehearing should be granted.

Respectfully submitted,

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I hereby certify that the foregoing petition for rehearing is presented in good faith and not for delay and is restricted to grounds specified in Rule 58 of the Rules of this Court.

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